So You Moved Out of Illinois! Are You Sure?

by Paul Bogdanski, David P. Dorner, and Jeremy P. Gove

Paul Bogdanski

David P. Dorner

Jeremy P. Gove

Paul Bogdanski and David P. Dorner are partners with Reed Smith LLP in Chicago, and Jeremy P. Gove is an associate in the firm's New York office.

In this installment of Insights From Former Insiders, the authors discuss Illinois's requirements for establishing domicile in another state.

It is not unusual for people to relocate from Illinois to states with warmer climates and lower income taxes, such as Florida, Tennessee, Texas, and others. In connection with their move, they may buy or lease a home, apply for a new driver's license, register to vote, and possibly even file some form of declaration of residency with their new home state. For many people this is sufficient evidence of their move from Illinois for state income tax purposes. However, for high-net-worth individuals, more is often required to prove a change of residency.

Over the last 15 years, the Illinois Department of Revenue has regularly audited high-net-worth individuals who claim to have shifted their residence from Illinois to a low- or no-personal-income-tax state. The DOR often focuses its audit efforts on individuals who accumulated significant wealth while living in Illinois and then shifted their residence to a low-tax state, or individuals who had a significant income recognition event (for example, the sale of a business) shortly after shifting their residence from Illinois. While it is perfectly acceptable to change one's domicile for the primary purpose of tax planning, taxpayers must be careful to comply with the requirements for establishing domicile in another state. Such a change should be documented with admissible books and records.

Often, a former Illinois resident will maintain significant ties with Illinois, through the ownership of a former family home, an interest in an Illinois business, or through other investments connected with the state. They may also retain membership in Illinois country clubs and other Illinois-based civic, social, and religious organizations. It is also common for one spouse to move to another state while the other spouse remains a resident of Illinois to be closer to a parent, children, grandchildren, or friends. In these circumstances, the former Illinois resident may still make visits to the state on a frequent basis. Accordingly, while a high-net-worth individual may intend to terminate his or her Illinois residency, their unique circumstances, including the ownership of multiple homes and engaging in frequent travel, could lead the DOR, and possibly a court, to reach a different conclusion.

Under Illinois law, an individual is a resident of Illinois for income tax purposes if (1) the individual is in Illinois for other than a temporary or transitory purpose, or (2) the individual's domicile is in Illinois but he or she is absent from the state for a temporary or transitory purpose.[1] Generally, a person's presence is "temporary" or "transitory" if the person's visit to a state is for a fixed or limited duration (that is, not indefinite) and the person has the intent to leave the state after the purpose of being there is completed. A resident of Illinois is usually, but not always, domiciled in Illinois. The term "domicile" commonly means an individual's "permanent home," which is where the individual intends to return after a period of absence.[2] In other words, it is the place where you are when you have no reason to be someplace else. An individual has only one domicile and does not acquire a new domicile without first abandoning their prior domicile.[3]

The outcome of a residency case often depends on whether the individual is absent from Illinois for other than a temporary purpose, but it is often discussed in terms of whether the individual has established a domicile outside Illinois. The parties and the courts typically focus on domicile because a temporary absence from one's domicile does not generally create residency someplace else. For instance, if an individual maintains two homes — one in Illinois and a second in Florida — and the individual spends a substantial amount of time in each home, then, for tax purposes, the individual will almost always be a resident of the state in which he or she is domiciled, because the individual's activities in the other state will generally be viewed as transitory or temporary in nature.[4]

An individual's place of domicile, and ultimately his or her residency status, is generally a matter of intent — that is, the intent to create a new domicile in another state (or country) or the intent to remain in a state for other than a temporary or transitory purpose. Whether an individual intends to be present in Illinois for only a temporary or transitory purpose is evidenced by the facts and circumstances specific to each situation. However, there is a statutory presumption in Illinois that an individual is a resident of Illinois if he or she claims a homestead exemption for real property in the state. There is also a presumption that an individual who is an Illinois resident in one year is a resident in the following year, if during the following year he or she is present in Illinois for more days than in any other state.[5]

Starting in 2010, a string of Illinois cases were resolved in favor of individuals contesting their Illinois residency.[6] As a result, lengthy rounds of discovery in Illinois residency cases became the norm. To secure a more detailed understanding of a taxpayer's intent to be domiciled outside Illinois, the DOR's attorneys commonly issue detailed discovery requests, and in some cases even issue subpoenas. The voluminous discovery typically focuses on the taxpayer's credit card records to determine the location of their activities and purchases, the frequency of their travel to and from Illinois and other locations, their social or other club memberships, and even their philanthropic endeavors. In more recent years, the DOR's auditors have begun to request the same sort of detailed information at audit that the department's attorneys have been seeking in discovery.

Below is a sample of the more detailed requests for documentation that an individual taxpayer can expect to receive in connection with an Illinois residency audit resulting from a move from Illinois to another state (the destination state):

1. A list of days that the taxpayer either arrived in or departed from Illinois, along with the corresponding origin/destination, and the purpose of each trip.

2. A list of days (by date) that the taxpayer either arrived in or departed from the destination state, along with the

[1] 35 Ill. Comp. Stat. 1501(a)(20).

[2] Ill. Admin. Code tit. 86, section 100.3020(d).

[3] *Id*.

[4] *See Dods v. Department of Revenue*, Cook County Case No. 07 L 050695 (Aug. 24, 2009), *aff'd*, 402 Ill. App. 3d 1179 (Rule 23 Order, Aug. 19, 2010).

[5] Ill. Admin. Code tit. 86, section 100.3020(f).

[6] *See, e.g.*, *Cain v. Hamer*, 2012 IL App. (1st) 112833 (July 16, 2012); *Grede v. Hamer*, 2013 Ill. App. 2d 120731-U (Apr. 22, 2013); *Dods v. Hamer*, 402 Ill. App. 3d 1179 (Rule 23 Order, Aug. 19, 2010); and *Sweeney v. Hamer*, Cook County Circuit Court Order, Case No. 10-L-050524 (June 26, 2013).

corresponding origin/destination, and the purpose of each trip.

3. A daily calendar copy (for example, Outlook) for the taxpayer.

4. Copies of all automobile moving violations received in the state of Illinois and/or the destination state during the audit period.

5. Copies of all "official" records detailing date/geographic charges for any I-PASS/E-ZPass to which the taxpayer had access or used during the audit period (as a driver or passenger).

6. A list of any/all social clubs, including athletic clubs, country clubs, fraternities, and religious organizations, in which the taxpayer was a member during the audit period, including the location and the taxpayer's membership status for each organization.

7. Copies of any monthly/annual membership statements/newsletters from any social clubs, including athletic clubs, country clubs, fraternities, and religious organizations, in which the taxpayer was a member during the audit period.

8. A list of all judicial proceedings to which the taxpayer was a party or in which the taxpayer participated as a representative or witness during the audit period.

9. A copy of the taxpayer's official third-party credit report (scores, balances, and late payments may be redacted).

10. A copy of the monthly credit/bank card statements for any/all credit or bank cards that the taxpayer had access to or used.

11. A narrative describing the specific circumstances surrounding the taxpayer's decision to claim the destination state as his or her state of domicile.

It has been said that "you can't steal second base and keep your foot on first,"[7] and that concept applies to creating a new domicile. Often, taxpayers will ask what they need to do to terminate their Illinois residency. The answer is simple: move. However, moving from Illinois does not necessarily mean severing all ties with the state and never being able to visit grandchildren or friends in the state again. It does not even require the sale of your Illinois home. After establishing residency outside Illinois, you can return to Illinois for extended periods or on a regular basis. However, these visits must be temporary, and you must be able to demonstrate that after each visit you plan to return to your new domicile. Taxpayers must also be aware that each extended visit to Illinois may raise additional scrutiny from the DOR regarding whether he or she is still a statutory resident of Illinois, regardless of where the taxpayer is domiciled.

What you cannot do, though, is claim you moved to another state while doing the bare minimum to establish a domicile in the other state. The DOR will look deeper into your intent to actually move from Illinois, such as whether you moved your "near and dear" items (such as pictures, important papers, keepsakes, etc.) to your new state. Thus, the basic facts used to demonstrate a change of residency, such as getting a driver's license and registering to vote in the destination state, are no longer sufficient in Illinois, at least not for high-net-worth individuals.

The detailed nature of the information requested by the DOR in a typical residency audit should put high-net-worth individuals on notice that they cannot venture lightly when moving from Illinois. Sufficient thought and effort, and consultation with a tax professional, are necessary to establish and document a change of residency, and to obtain the desired tax result: clearly ending up on second base. In short, the department has upped its residency audit game, and so should you. ■

[7] Attributable to Frederick Wilcox.