BNA ARTICLE: WHAT YOU NEED TO KNOW ABOUT FLORIDA LAW TO ADVISE YOUR CLIENTS WHO LIVE HERE

By Alan S. Gassman, Esquire

> *"My parents didn't want to move to Florida, but they turned sixty and that's the law."* - Jerry Seinfeld
>
> "*I was just heading down to Buckhead to get the newspaper and the next thing I knew I was on I-95 heading for Florida.*" - Jimmy Buffet

INTRODUCTION:

A great many lawyers, CPAs, and financial advisors have clients who reside in Florida or spend a good deal of time there and have the need to know about a number of unique Florida laws that can significantly impact individuals and businesses there.

These include many rules beyond typical will and trust laws, which lawyers throughout the country can navigate when their clients move to Florida or have a substantial presence in Florida. Florida has restrictive constitutional homestead disposition limitations, a unique elective share statute, documentary stamp taxes that can even impact transfers between spouses or to wholly owned entities, vehicle liability rules, and creditor protection statutes and case law that would often not be expected by someone who is not familiar with Florida's unique laws.

This outline is intended to provide non-Florida lawyers, trust officers and financial advisors with important information that will apply to Florida clients and can significantly impact planning design and implementation. It's not just alligators, mosquitoes and sharks that can bite clients and their advisors!

Over 300 hours was spent researching and writing this outline. The author sincerely thanks Stetson Law School students Carly Ross, Eric Moody, and Kacie Hohnadell, and recent Stetson Law School graduate Alexandra Fugate, as well as law partners Kenneth Crotty, Esq. and Christopher Denicolo, Esq. for all of their work, comments, and contributions to this outline and predecessor materials that have been used to complete this. Also, property and casualty insurance agent, Chuck Wasson, and elder law attorney, Charlie Robinson, made substantial contributions to this work.

Part II of this article will appear in the _______ Edition of ______________ and will cover many topics, including Florida required inheritance rules with respect to homestead, elective share avoidance techniques, and unique creditor protection opportunities and traps for the unwary. Stay tuned!

Our 2013 Florida Advisor Calendar Checklist

Filing period for annual reports of Corporations, LLC, LLP, LP and non-profit	January 1 - May 1
Gasparilla Pirate Festival in Tampa	January 26
Deadline for purchasing a Florida 529 Prepaid College Plan at the previous year's prices	January 31
Spring Break	February 23 - April 20
Homestead application deadline	March 1
Bike Week in Daytona Beach	March 8-17
Florida Corporate Income Tax Due	March 15 - April 1
Hurricane Season	June 1 - November 30
Fantasy Fest in Key West	October 18-27
First day of Hanukkah (time to buy a gift for your Jewish tax lawyer)	November 27
Deadline for early payment of Property Taxes with a discount (check your county tax appraiser's website for the exact deadlines)	4%......................November 30 3%......................December 31 2%......................January 31 following year 1%......................February 28 following year
Property Tax deadline	Typically March 31, but check your tax appraiser's website to be sure
TRIM Notice - Right to contest an appraisal	Varies - see your tax appraiser's website immediately after you receive notice
Vehicle Tag Renewal	Annual on the owner's birthday
Open Enrollment for HMOs	Varies - Check with your Employer's human resource department

A Very Treacherous New Durable Power of Attorney Act

In 2010, the Florida Legislature revamped its Durable Power of Attorney statute in several ways (Chapter 709 of the Florida Statutes).

A Durable Power of Attorney form and a form to use to facilitate and escrowed Power of Attorney with optional clauses is attached at the end of this Article.

The new law specifically prohibits the use of "springing powers of attorney" executed after September 30, 2010, meaning that powers of attorney signed after that date which provide that they have no effect until the incapacity of the principal will have no force whatsoever. Although springing powers of attorney signed prior to Oct. 1, 2011 are grandfathered in, they will now only be enforceable if the agent receives a letter signed by the principal's primary Florida doctor attesting to incapacity. The new law also requires that any power of attorney signed after the above referenced date contain explicit authority for each action that an agent would take. A general authorization of power will not be enforceable.

Also, many powers and authorities will not be effective in a post-September 30, 2011 power of attorney unless the principal separately initials or signs specific places below seven separately enumerated categories of powers, which include giving the agent the power to: (1) Create an inter vivos trust; (2) Amend, revoke, or terminate a trust created by or for the benefit of the Principal; (3) Create or change rights of survivorship; (4) Create or change a beneficiary designation; (5) Waive the Principal's rights to be a beneficiary of a joint and survivor annuity, including a survivor benefit under a retirement plan; (6) disclaim property or powers of appointment; and (7) Make a gift as described in Florida Statute Section 709.2202(3).

The new statute also provides that an agent is not eligible to be compensated for the services rendered unless one of the following applies:

1. The agent is the spouse or an heir of the principle.

2. The agent is a Florida resident that has never been an agent for more than 3 principles at the same time.

3. The agent is a Florida licensed lawyer or CPA.

4. The agent is a financial institution that has Florida trust powers.

6 Catastrophes That Can Happen as a Result of the New Florida Durable Power of Attorney Act

1. Signing a springing power of attorney: will have no force or effect after Sept. 30, 2011.

2. Not enumerating each and every power that the Agent will need to exercise, in that a general authorization provides no power or authority - specific enumeration is required for a post-September 30th Power of Attorney.

3. Authorizing the agent to conduct certain actions, without separately signing or initialing each provision, will not be sufficient to allow the agent to do any of the following:

a. Create an inter vivos trust (living trust): the terms of the trust agreement may prevent amendment or termination by an agent under a power of attorney

b. Amend, revoke, or terminate a trust created by or for the benefit of the principal (if the trust instrument allows it)

c. Make a gift subject to § 709.2202(3)

d. Create or change rights of survivorship

e. Create or change a beneficiary designation

f. Waive the principal's rights to be a beneficiary of a joint and survivor annuity, including a survivor benefit under a retirement plan

g. Disclaim property or powers of appointment

4. Executing a power of attorney after September 30, 2011 without having two witnesses and a notary to each signature.

a. Before October 1,2011, two witnesses would be sufficient if the power of attorney is not a "durable power of attorney," or if the agent will not be transferring real estate or signing other documents that require notarization and "equal dignity."

b. Note: Healthcare powers of attorney require that the two witnesses not be related to the person giving the power.

5. An agent is not eligible for compensation, unless: 1) the agent is the spouse or an heir of the principle; 2) The agent is a Florida resident that has never been an agent for more than 3 principles at the same time; 3) The agent is a Florida licensed lawyer or CPA; or 4) The agent is a financial institution that has Florida trust powers.

How Many illegal contracts will be entered into as a result of this?

6. Granting someone a power of attorney that you do not trust 100%.

Untrustworthy agents may seek to have principals sign new powers of attorney because of recent articles and publicity, and will then take advantage of them.

Health Care Powers of Attorney Witness and Notarization Requirements.

The signing of a health care power of attorney must be witnessed by two individuals who are not relatives of the principal, and also must be notarized.

The health care power of attorney document is attached as Exhibit ___.

FLORIDA TAX LAW

No Individual, Partnership, S Corporation, or Trust Income Taxes or Tax Returns!

Florida has no individual, partnership, S corporation, or trust income taxes, but does impose sales tax on sales and rentals of many items, a 5% income tax on C corporation income, documentary stamp taxes on real estate transfers and mortgages, and intangible taxes on borrowing.

Florida's Constitution prohibits a state income tax and would be very difficult to amend.

Florida had an intangibles tax which was based upon the value of stocks, mutual funds and bonds other than Florida municipal bonds. This tax was reduced to $1.50 per $1,000 of value of non-exempt intangible assets in 1999, and was eliminated beginning in 2007.

Because there are no individual income taxes or S corporation taxes, Florida imposes a number of other taxes and charges which many people from other states are not accustomed to seeing, and a number of planning considerations and tax uncertainties are discussed below.

The Florida Department of Revenue is said by many to have aggressive and inflexible auditors and revenue agents, while the advisory staff in Tallahassee is said to be much more reasonable and informative. Taxpayer advisory opinions cost nothing to request, so oftentimes it is better to ask permission than forgiveness when contemplating state tax associated conduct.

No Inheritance or Estate Taxes.

Previously, Florida had a "pickup tax" that was imposed upon estates of Florida residents. This tax was coined a "pickup tax" because Florida essentially "picked up" all, or a portion of, the amount of the credit for state death taxes allowed on the federal estate tax return. On December 31, 2004, the federal law changed to make the federal credit a deduction for state estate taxes, which eliminated Florida's pickup tax. Although the tax was eliminated, estates are still required to file an Affidavit of No Florida Estate Tax Due with the state of Florida, regardless of whether the estate is required to file a Form 706 or 706NA Federal Estate Tax Return. The probate estates of decedents required to file the Federal Estate Tax Return cannot be closed, according to most probate judges, unless or until a Closing Letter is received from the Internal Revenue Service. Where there are modest estate tax returns to facilitate allowing a surviving spouse to have portability of unused estate tax exemption, it may be necessary to keep the probate estate open until a clearance letter is received from the Internal Revenue Service. This will be a further burden of filing an estate tax return for a modest estate. Hopefully a probate judge will permit the closure of an estate before a clearance letter is received, where the estate tax return was filed voluntarily and not by reason of being required by the Internal Revenue Service.

C Corporation and Business Taxes

Florida does impose a 5.5% income tax on the net income of C corporations, making S corporations and partnerships more attractive comparably than C corporations for business and investment activities in Florida. C corporations that zero out income each year by paying compensation to officers and directors will pay no tax in Florida unless deductions for compensation or other expenses are disallowed. A Florida limited liability company that elects to be treated as a C corporation for Federal income tax purposes will be subject to Florida income tax accordingly.

Tangible Taxes

Businesses pay a tangible personal property tax based on the value of their physical non-real estate assets. The millage, or rate of taxation, is set by the Board of County Commissioners, School Board, City Council and governing bodies of other independent special taxing districts and authorities. The millage is set by calculating a rate per $1,000 valuation that will produce the county's budget needs from ad valorem taxes. One mill represents $1 of tax on each $1,000 of taxable valuation. The tax rates typically range from approximately 15 to 20 mills (15-20% of the value of physical business assets).

Unemployment Tax

Renamed the "Reemployment Tax" in the 2012 legislative session, Florida's unemployment tax requires employers to pay a tax based on wages of their employees as part of efforts to help Florida's job seekers get reemployed. The rate for initial employers is 2.7% of payroll for the first 10 quarters (based on the employees' annual salary up to $8,000). After that, the rate is recalculated based on the employer's history, with a maximum rate of $432 a year per employee.

Workers' Compensation

In addition to the above taxes, Florida employers who employ four or more part or full time employees are also required to obtain workers' compensation coverage. The rates vary and are dependent on the business's industry classification, its history of workers' compensation claims, salaries paid to employees, and other factors. Chapter 440, F.S., establishes workers' compensation coverage requirements for employers. If an employer is unable to obtain coverage through the private insurance market, the employer can contact the Florida Workers' Compensation Joint Underwriting Association at (941) 378-7400.

<u>Sales Tax on the Sale of Tangible Assets and Rentals</u>

A 6% general sales tax applies statewide. In addition, most counties in Florida apply a discretionary sales surtax on top of that. County surtax rates currently range from .5% to 1.5%, but 40 out of 67 Florida counties have a 1% addition and a consequent 7% sales tax. Below is a chart from the Florida Department of Revenue with each county's total sales tax rate.

Discretionary Sales Surtax Rates for 2012

COUNTY	TOTAL SURTAX RATE		EFFECTIVE DATE	EXPIRATION DATE
Alachua	**None**			
Baker	1%		Jan 1, 1994	None
Bay	.5%		Jan 1, 2011	Dec 2020
Bradford	1%		Mar 1, 1993	None
Brevard	None			
Broward	None			
Calhoun	1.5%	(1%)	Jan 1, 2009	None
		(.5%)	Jan 1, 2009	Dec 2018
Charlotte	1%		Jan 1, 2009	Dec 2014
Citrus	None			
Clay	1%		Feb 1, 1990	Dec 2019
Collier	None			
Columbia	1%		Aug 1, 1994	None
Dade	See Miami-Dade for rates.			
De Soto	1%		Jan 1, 1988	None
Dixie	1%		Apr 1, 1990	Dec 2029
Duval	1%	(.5%)	Jan 1, 1989	None
		(.5%)	Jan 1, 2001	Dec 2030
Escambia	1.5%	(1%)	Jun 1, 1992	Dec 2017
		(.5%)	Jan 1, 1998	Dec 2017
Flagler	**1%**	**(.5%)**	**Jan 1, 2003**	**Dec 2012** ←
		(.5%)	**Jan 1, 2003**	**Dec 2012** ←
Franklin	1%		Jan 1, 2008	None
Gadsden	1.5%	(1%)	Jan 1, 1996	None
		(.5%)	Jan 1, 2009	Dec 2038
Gilchrist	1%		Oct 1, 1992	None
Glades	1%		Feb 1, 1992	Dec 2021
Gulf	1%		Jan 1, 2010	None
Hamilton	1%		Jul 1, 1990	Dec 2019
Hardee	1%		Jan 1, 1998	None
Hendry	1%		Jan 1, 1988	None
Hernando	.5%		Jan 1, 2005	Dec 2014
Highlands	1%		Nov 1, 1989	Oct 2019
Hillsborough	1%	(.5%)	Dec 1, 1996	Nov 2026
		(.5%)	Oct 1, 2001	None
Holmes	1%		Oct 1, 1995	Dec 2013
Indian River	1%		Jun 1, 1989	Dec 2019
Jackson	1.5%	(1%)	Jun 1, 1995	Dec 2025
		(.5%)	Jul 1, 1996	Dec 2015
Jefferson	1%		Jun 1, 1988	None
Lafayette	1%		Sep 1, 1991	None
Lake	1%		Jan 1, 1988	Dec 2017
Lee	None			
Leon	**1.5%**	**(1%)**	**Dec 1, 1989**	**Dec 2019**
		(.5%)	**Jan 1, 2003**	**Dec 2012** ←
Levy	1%		Oct 1, 1992	None
Liberty	**1.5%**	**(1%)**	**Nov 1, 1992**	**None**
		(.5%)	**Jan 1, 2012**	**Dec 2020**
Madison	1.5%	(1%)	Aug 1, 1989	None
		(.5%)	Jan 1, 2007	None
Manatee	.5%		Jan 1, 2003	Dec 2017
Marion	None			
Martin	**None**			
Miami-Dade	1%	(.5%)	Jan 1, 1992	None
		(.5%)	Jan 1, 2003	None
Monroe	1.5%	(1%)	Nov 1, 1989	Dec 2018
		(.5%)	Jan 1, 1996	Dec 2015
Nassau	1%		Mar 1, 1996	None
Okaloosa	None			
Okeechobee	1%		Oct 1, 1995	None
Orange	.5%		Jan 1, 2003	Dec 2015
Osceola	1%		Sep 1, 1990	Aug 2025
Palm Beach	None			
Pasco	1%		Jan 1, 2005	Dec 2014
Pinellas	1%		Feb 1, 1990	Dec 2019
Polk	1%	(.5%)	Jan 1, 2004	Dec 2018
		(.5%)	Jan 1, 2005	Dec 2019
Putnam	1%		Jan 1, 2003	Dec 2017
St. Johns	None			
St. Lucie	.5%		Jul 1, 1996	Dec 2026
Santa Rosa	.5%		Oct 1, 1998	Dec 2018
Sarasota	1%		Sep 1, 1989	Dec 2024
Seminole	**None**			
Sumter	1%		Jan 1, 1993	None
Suwannee	1%		Jan 1, 1988	None
Taylor	1%		Aug 1, 1989	Dec 2029
Union	1%		Feb 1, 1993	None
Volusia	.5%		Jan 1, 2002	Dec 2016
Wakulla	1%		Jan 1, 1988	Dec 2017
Walton	1%		Feb 1, 1995	None
Washington	1%		Nov 1, 1993	None

Each county that has a surtax levy that is new, revised, or extended is indicated in bold. Any county that has a surtax that expires in 2012 is also in bold and has an ← beside the expiration date.

This sales tax does not apply to the “isolated sale” of business assets where no business broker is involved with the sale, under the exceptions in rule 12A-1.037 of the Florida Administrative Code which states that “[t]he sale of business assets in conjunction with the sale of the business... other than inventory and aircraft, boats, mobile homes and motor vehicles, qualifies as an isolated sale provided the sale and the transfer of the assets of the business is completed within thirty (30) days from the date of the agreement for the sale of the business.” The rule also states that if there is a business broker, agent or auctioneer involved with the sale, the exception above does not apply on the theory that the sale is not isolated, so sellers of businesses should be made aware of this issue. This tax would not apply when the stock of a company is sold as opposed to an asset sale. Florida also does not have a Bulk Sales Act.

Florida has an annual “back to school” three-day sales tax holiday each year in August where no sales tax is collected on clothing, footwear and certain accessories ($75 and under per item) as well as school supplies that are $15 and under per item.

Sales Tax On Rent

The sales tax also applies to rent, even when paid between related entities, and the Florida Department of Revenue has been known to take the position that rent will be considered as paid in almost any instance where monies pass directly or indirectly between related entities with a lessor/lessee relationship. Also, if the “tenant” pays mortgage payments on behalf of the real estate entity, the Department will take the position that this is rent according to Technical Assistance Advisement 10A-026. This has been known to occur even when the operating entity makes distributions to its shareholders and the shareholders separately make contributions to the capital of the real estate company, although there are older Technical Assistance Advisements which would indicate that this does not necessarily need to be the case. Technical Assistance Advisement 07A-011, for instance, points out that the Department has previously recognized that there may be situations wherein “income” or “profit” flowing between related entities would not be “rental consideration.”

Because the statute of limitations on sales tax never runs unless and until a sales tax return has been filed, many taxpayers pay a small amount of rent or lease a small part of the property to another user and pay sales tax and file returns.

Many taxpayers will not be able to deduct interest and depreciation from rental activity that would otherwise be available because of the passive activity loss rules. IRC § 469(c)(7) may nevertheless permit these deductions where a “tenant entity” and the real estate owner entity have generally identical ownership, and the real estate is used in the tenant’s trade or business.

IRC § 469(c) directs that activities may be treated as a single activity if they constitute an appropriate economic unit for the measurement of gain or loss for purposes of § 469. If the rental activity can be grouped to the taxpayer’s trade or business activity, they can avoid the passive loss rules which limit deductibility.

Treas. Reg. § 1.469-4(c)(2) lists five nonexclusive factors which are to be given the greatest weight in determining whether activities constitute an appropriate economic unit: (i) Similarities and differences in types of trades or businesses; (ii) The extent of common control; (iii) The extent of common ownership; (iv) Geographical location; and (v) Interdependencies between or among the activities.

Section 1.469-4(d)(1)(i) further provides that even where a rental activity and a trade or business activity constitute an appropriate economic unit, they may be grouped together only if one of the following three elements are met: (A) The rental activity is insubstantial in relation to the trade or business activity; (B) The trade or business activity is insubstantial in relation to the rental activity; or (C) Each owner of the trade or business activity has the same proportionate ownership in the rental activity, in which case the portion of the rental activity that involves the rental of items of property for use in the trade or business activity may be grouped with the trade or business activity.

The author is not sure why the word "insubstantial" is contained in the regulation, or what it is intended to mean. The Treasury Regulations do not define the term "insubstantial" and there is very little case law addressing this issue. In *Candelaria v. United States*, 518 F.Supp.2d 852 (W.D. Tex. 2007), the court attempted to craft a definition of this term. The court found that in determining insubstantiality, the analysis should focus on "pertinent factors" including the following: the relationship of income between the rental activity and business activity (using the 80/20 rule); whether the entities work together as a single business unit rather than two distinct entities; and whether the rental activity was created solely for the other business entity's benefit.

Florida imposes sales tax on residential rentals, known as "transient accommodations, " unless there is a bona fide written lease for a period of longer than 6 months. Florida Administrative Code Rule 12A-1.061 provides that in order to be considered a lease for a period longer than six months, a written lease agreement effective the first day of a month must run through the first day of the seventh consecutive month, and a lease starting at any other day in the month must be in effect until the day after the corresponding day of the seventh month. For example, a lease agreement effective July 1st must be effective through January 1st, and a lease effective July 28th must be effective through January 29th. For a written lease to be considered "bona fide" it cannot contain a provision allowing the lessee to cancel the lease at any time without penalty or a provision that would allow the lessee to avoid full payment of the stated amount of the rent. Any lease for one or more years must be in writing with two witnesses to each signature in order to be enforceable.

Years ago, there was a loophole that provided that no sales tax would be due on the mortgage payments made by the tenant if the tenant was a guarantor of the mortgage debt. This loophole was legislated out of the law several years ago, but some practitioners and taxpayers are not aware that they have significant exposure for sales tax on ongoing rent payments.

The sale of a motor vehicle, airplane, boat, or other titled transportation vehicle occasions the requirement to pay a 7% sales tax, and the Florida Department of Revenue has been known to actively track physical airplanes and boats to check to see whether sales tax was paid when they were acquired by out of state companies or other entities that Floridians are sometimes erroneously advised to set up and maintain to attempt to avoid these taxes.

Sales tax is also due when a vehicle, boat, or airplane is transferred to or from a wholly owned or brother/sister company or other limited liability entity, partnership or corporation, even where there is no consideration. In these types of transfers, consideration is presumed according to Fla. Admin. Code Rule 12A-1.007(25)(d).

Rule 12A-1.007(25)(b)(2) indicates that the transfer of title as a gift into a revocable or irrevocable trust is also not taxable. The pertinent language is as follows:

> The transfer of title as a gift into a revocable or irrevocable trust is not taxable. A transfer subject to a lien(s) will not qualify as a gift when any outstanding lien(s) is assumed by the trust.

As discussed in the Trust Section of this article, many planners now use irrevocable trusts to limit liability for investment properties and activities while avoiding sales taxes on transfers to the trust entity, documentary stamp taxes on conveyances of real estate, and the extra premiums or lower liability insurance coverages offered for corporate owned real estate by many insurance carriers in Florida.

Documentary Stamp Tax on Real Estate Transfers

In addition, many Floridians are surprised to learn that they have to pay a 7/10 of 1% documentary stamp tax on the transfer of real estate. This tax does not apply to gifts of real estate, but if real estate is gifted subject to a mortgage, the amount owed on the mortgage will be deemed consideration, subject to the 7/10 of 1% tax.

Documentary stamp tax is also not applicable in a bankruptcy proceeding, so it is not unusual to find borrowers and lenders going to legal counsel to obtain a “pre-packaged bankruptcy” arrangement, when property is given to a lender as a “deed in lieu of foreclosure.” This process can also enable the debtor to avoid taxable income from the discharge of indebtedness under Internal Revenue Code Section 108.

The Department of Revenue regularly checks deeds that have been recorded where documentary stamp tax has not been paid, particularly where there is a mortgage on the property that has been ignored in the determination of documentary stamp tax amount and reporting.

Typically the Department of Revenue will accept the tax assessor value of the property to determine the documentary stamp tax where that is greater than the mortgage balance. Before the 2007-2008 real estate crisis, tax assessor values were commonly 75-80% of the “real fair market value” of real estate, but at the present time we most commonly find that the tax assessor “just value” is at or within 5% of the correct market value.

Many married couples are surprised to learn that they have to pay a documentary stamp tax when property is transferred from one spouse to the other (or other spouse's trust), or from joint names to an individual name. This is because the "shift in mortgage responsibility" is considered taxable. For example, a married couple with joint ownership of a property subject to a $200,000 mortgage would pay documentary stamp tax based upon $100,000 if the property were transferred from both spouses to one spouse. The author does not know whether this tax could be avoided by stating in the deed or by separate agreement that the conveying spouse will remain wholly or equally liable on the underlying indebtedness. The Department of Revenue routinely reviews deeds and sends notices of tax, interest and penalties due when real estate is conveyed subject to a mortgage and no documentary stamp tax is paid.

When unencumbered real estate is transferred to a company owned solely and in the same percentages as the real estate transferor or transferors, documentary stamp tax will not be imposed based upon the rationale that there is not consideration for the transfer. This is the result of the Florida 2nd District Court of Appeal decision of *Kuro Inc. v. State Dept. of Revenue*, 713 So. 2d 1021 (Fla. 2d DCA 1998), which was affirmed by the Florida Supreme Court in *Crescent Miami Center, LLC v. Florida Dept. of Revenue,* 903 So. 2d 913 (Fla. 2005).

After the *Kuro* and *Crescent Miami Center* opinions were released, many planners avoided documentary stamp tax by first having clients convey property to identically owned LLCs and then transferring ownership in the LLC to an arms-length purchaser or other parties. The step transaction doctrine has never been applied in a Florida tax case, and apparently does not apply in Florida taxation matters.

To partly close this loophole, the Florida Legislature passed Florida Statute Section 201.0201 in 2009, which provides that the transfer of an LLC interest that corresponds to real estate transferred to the LLC within three (3) years will be considered to be a documentary stamp taxable sale, unless the transfer is within an exception.

The exceptions include: (1) the transfer of an LLC interest to a trust that is disregarded for federal income tax purposes; and (2) a gift transfer of the LLC interest where there is no consideration.

Documentary stamp tax will, however, be due on a transfer of real estate that is encumbered by debt. Florida Statute Section 201.0201 specifically limited the effect of *Kuro* and *Crescent Miami Center* to transfers of unencumbered property so that a taxable sale is considered to have occurred to the extent of indebtedness when an exception would otherwise apply.

Converting Co-Ownerships to LLC or other Entity Ownership.

The Florida conversion statute permits a general partnership to convert into a limited liability company, limited liability partnership, limited partnership, or limited liability limited partnership without the need to retitle the real estate by deed, although the articles of conversion are typically recorded in the court house records, and oftentimes a warranty deed from the name of the former entity to the name of the new entity will be prepared and recorded in order to avoid having confusion on the public records. Typically we use warranty deeds instead of quit claim deeds because most title insurance policies will benefit a subsequent owner who acquires title by warranty deed, but not if subsequent title is acquired by quit claim deed.

Where partners own real estate directly or under a general partnership, the entity can be converted into a limited liability company without the payment of documentary stamp tax. Co-owners of real estate who consider themselves to be partners in a partnership may therefore be able to convert the individual co-ownership into a limited liability company ownership without paying documentary stamp tax, although Department of Revenue personnel can be expected to ask for copies of previously filed partnership income tax returns (Form 1065) and of a written general partnership agreement, although these do not seem to be necessary. Co-owners of property who engage in a reasonable level of business activity can be considered to be partners. Florida courts have routinely held that in order to form a partnership, there must be a contribution by both parties "to the labor or capital of the enterprise, . . . a mutuality of interest in both profits and losses, and an agree[ment] to share in the assets and liabilities of the business." *Williams v. Obstfeld*, 314 F. 3d 1270, 1275 (11th Cir. 2002), quoting *Dreyfuss v. Dreyfuss*, 701 So. 2d 437, 439 (Fla. DCA 1997); *see Jackson-Shaw Co. V. Jacksonville Aviation Authority*, 510 F.Supp.2d 691, 727 (M.D. Fla. 2007).

Sometimes the transfer will be to the Trustee of a land trust owned by the successor entity so that there can be confidentiality in the public records with respect to the successor ownership and less chance of a Department of Revenue review of the matter from a stamp tax standpoint. Transfers of real estate to a revocable trust or a typical land trust owned by the transferor will not trigger documentary stamp tax, but if the land trust is owned by another entity stamp taxes may be triggered based on whether a transfer to the owner entity would have triggered the tax.

Documentary Stamp Tax Imposed Upon an Issuance of Debt.

Florida also has a documentary stamp tax on the issuance of indebtedness, which is based on $0.35 per $100 of debt, but the stamp tax on debt not secured by a mortgage is capped at $2,450, so there is no documentary stamp tax on SUCH debt exceeding $1,285,710. The tax is payable by any of the parties to a taxable transaction.

A promissory note issued in Florida cannot be enforced in court unless or until the documentary stamp tax has been paid, but late payment of the tax will be permitted.

One Time Intangible Tax Imposed Upon Issuing Real Estate Mortgages.

Where the debt is secured by a mortgage on Florida real estate, there is no way to avoid this tax, and an additional 2/10 of 1% state intangible tax is also charged on the mortgage itself, bringing the cost of mortgage borrowing to 55/100 of 1% for the first $2,450 of mortgage debt, and 2/10 of 1% for amounts exceeding that. The tax is not imposed on security interests granted in entities that own real estate, as discussed below.
As a result of the above, the total taxes imposed on mortgage borrowing are based upon .55% of the amount loaned.

One way to avoid Florida intangible taxes imposed upon borrowing is by placing real estate under a Land Trust, LLC or other entity, and having a promissory note and a pledge or security agreement arrangement executed and delivered outside of Florida without a mortgage being placed on the property. While the lender cannot be assured that the borrowing entity cannot mortgage the property to give a superior lien to another lender, a security interest or pledge arrangement will give a family member full and complete LEGAL rights to any and all proceeds from a sale or encumbrance of the property, and if the property is the primary or designated secondary residence of the borrower, interest can be deductible under Internal Revenue Code § 163 as qualified residence interest.

Under Internal Revenue Code Section 163, qualified residence interest, which includes both interest on acquisition indebtedness and home-equity indebtedness, can be deductible if secured by a qualified (primary or designated secondary) residence. A secured debt is defined in Treas. Reg. § 1.163-10T as "a debt that is on the security of any instrument (such as a mortgage, deed of trust, or land contract) that makes the interest of the debtor in the qualified residence specific security for the payment of the debt." Therefore, a note secured by a valid pledge or lien upon ownership of a land trust or other "income tax disregarded entity" would be deductible, provided that the land securing it qualifies as a primary or secondary residence under the statute.

Section 163 provides that acquisition indebtedness is any indebtedness that is incurred in acquiring, constructing, or substantially improving a qualified residence and is secured by the residence, but this Section limits the amount of acquisition indebtedness to $1 million ($500,000 for a married individual filing a separate return). Qualified residence interest also includes home-equity indebtedness, which is indebtedness other than acquisition indebtedness, but this amount is limited to $100,000. The general view is that these deductions are in the aggregate, so interest on any amount of mortgage debt over the $1 million threshold will not be deductible if the debt is on a single loan. However, in 2009 Chief Counsel Memorandum 200940030, the IRS seemed to expand this view by allowing the home-equity deduction ($100,000) in addition to the $1 million cap in a single loan.

It is also important to note that a "qualified residence" is the taxpayer's principal residence and one other dwelling the taxpayer uses as a residence during the year, which means that interest can be deductible on two residences. For example, interest is deductible on a mortgage secured by a taxpayer's principal residence and a vacation home that a taxpayer uses as a personal residence for a certain amount of time during the year.

Some lenders have been willing to accept unrecorded mortgages as stand by collateral for promissory notes, whereby the lender receives the signed mortgage document and has the right to record it if and when circumstances reflected in a Loan Agreement occur. Typically, the tax is due at the time of recording but Florida Administrative Code Rule 12.C-2.005 provides that if "there is no written instrument, or if the written instrument is not presented for recordation, the nonrecurring tax of two mills is due and payable within 30 days following the creation of the obligation."

Why Many Loan Closings Are Performed on Boats and Airplanes

Where there is not a mortgage on Florida real estate, the documentary stamp tax can be avoided by having the promissory note signed and delivered to the lender outside of Florida. Often times large transactions are conducted on boats or airplanes outside of the territorial waters, or in the Atlanta airport. Sometimes clients will simply appoint agents to sign a promissory note on their behalf, and lenders will appoint agents to receive the promissory note outside of Florida.

Real Estate Taxes

Land owners are taxed annually based upon city and county taxes of approximately 2% of "tax assessed value" each year. Tax assessed value typically ranges from being based upon 75-90% of the actual "just market value" of a particular property. This tax is divided between the state, the county, and any applicable city where the property is located. Each person is allowed to declare one residence to be his or her homestead for property tax reduction purposes, if he or she truly resides there.

The homestead tax exemption allows $50,000 of value to not be taxed, and thus saves approximately $1000 a year in taxes. Additional small exemptions are available for widows or widowers, the disabled, disabled veterans who are 65 and older, low-income seniors who are 65 and older, and deployed members of the military.

More importantly, "exempt homestead" property has the benefit of a cap on increased value, which cannot exceed the lesser of 3% of the prior year's value or the increase in the consumer price index each year. And when values go down, the value resets at the lower amount. When property values go up, people who have owned homes in Florida for many years pay much less in property taxes than their neighbors. In addition, in order to protect older citizens who want to downsize their homes without paying more property tax than they have been, an amendment to the Florida Constitution passed in 2008 permits the lower value tax base to be "ported" to a subsequent home if certain rules are followed.

Ownership for purposes of the homestead property tax exemptions can include direct personal ownership, ownership under a revocable trust, and beneficial ownership under a lease for 98 years or longer. For example, property subject to a 99 year lease that has 52 years left to run will qualify for the homestead tax exemption.

Qualified Personal Residence Trust planning can be handled without loss of homestead exemption advantages, if during the retained use term and thereafter the Grantor has continued exclusive use rights, and after the retained use term, if the Grantor enters into a 98 year or longer lease with the QPRT, under which fair market value can be paid. Proper trust language providing residency and use rights under a trust can qualify for continuation or initiation of homestead tax status, and after the retained use term the Grantor can enter into an arms length lease that qualifies as a 98 year or longer lease, which may be terminable upon agreed events, to qualify for homestead exemption status under the Florida constitution and Florida Statute § 196.041. County property appraisers are generally willing to review submitted documents and offer comment or confirmation that the homestead exemption will continue before implementation. Other unique and potentially treacherous homestead related Florida laws are discussed below.

LEGAL INTEREST RATES, USURY LIMITS, AND SELF-CANCELLING INSTALLMENT NOTE THOUGHTS

Most loans made in Florida cannot bear interest above 18%, although certain loans exceeding $500,000 may bear an interest rate of up to 25% per annum. The law does not distinguish between corporations and individuals. Banking institutions are subject to other rules, however.

This caused many self cancelling installment note arrangements to violate usury laws when the interest rates where much higher than they are now, and if and when interest rates increase, this concern will again affect many self cancelling installment note structures.

By way of background, self-cancelling installment notes are often used for federal estate tax planning purposes, whereby a higher interest rate must be used, in exchange for which, the note can be forgiven upon death, if entered into when the lender has better than a 50% chance of living at least 12 months at the time the loan was entered into. If the lender lives for at least 18 months, then there is an irrevocable presumption that the 50% probability test in the preceding sentence was met. The note must be set to balloon before the lender's life expectancy, as of the date the loan is made. Because of the possibility that the seller may die during the course of the term, the note must bear interest at above the otherwise applicable federal rate or have an increase in principal to take into account the "risk premium" that the lender deserves.

Most of the recognized software programs for interest rate calculations show one interest rate to apply if the note is amortized with equal annual payments of principal and interest, and a higher rate to apply to an interest-only note with a 100% balloon upon maturity. The interest rate is lower with the amortizing note because less principal is owed and thus less forgiveness will occur on death during the term.

The interest rate for self-cancelling installment notes is based on the 7520 rates at the time the note is made. For example, an 85 year old lender in November 2012, where the 7520 rate is 1% with a life expectancy under Mortality Table 2000CM is 6.22 years, could sell assets in exchange for a 6 year note and the interest rate for an interest only note would be 13.683% while the interest rate for an amortizing note would only be 11.4546%.

During periods when the 7520 rate is higher, in some situations only an amortizing note could be used because the interest rate on a interest only self-canceling installment note would be too high.

As an alternative to the interest rates described above, it is possible to increase the principal of the note as the premium given to the lender in exchange for entering into the sale transaction.

According to one software program, a November 2012 self-cancelling installment note for the 85 year old mentioned above, a 1% interest rate could be used if the principal was increased by 38.7905% (a $1,000,000 note would instead be a $1,387,905 note) for an amortizing note, or by 212.5823% for an interest only note under the above example.

In situations where the 7520 rate is higher, this would avoid all usury concerns, but if the health of the lender improves dramatically, repayment of the note at the end of the term would cause his or her estate to actually grow instead of getting smaller, although it might be possible to swap the note for a lower principal/higher interest note if this is not part of a "step transaction" to pay the note off early.

See the article entitled "Interesting Interest Questions: Interest Rates for Intra-Family Transactions" by the Author and Floridians Jerry Hesch, and Christopher Denicolo, which was published in the 2011 BNA Tax Management Estates, Gifts, and Trusts Journal (Vol. 36, No. 2).

CREDITOR PROTECTION

Florida is world renowned for its generous creditor exemption laws which date back to the years well before air conditioning, where debtors would be assured the best new start possible if they would move here. The creditor exempt assets have no limits on value and are completely immune to levy, seizure, or garnishment. Nevertheless, there are many exceptions and traps for the unwary that must be understood by those who advise Floridians. We will first address homestead creditor protection, followed by certain protections codified in Florida's statutes, and tenancy by the entireties.

Homestead Creditor Protection

Homestead protection, which is embodied in the state constitution, is one such protection and perhaps one of the broadest homestead laws in the country.

In 1862, the U.S. Congress passed the Homestead Act, which enabled a head of household to claim ownership of 160 acres of public land that they had resided on and improved for 5 years, and the Florida Constitution has since provided for absolute creditor protection for an unlimited value of property outside of the city limits for up to 160 acres. The protected 160 acres can include non-homestead uses like owning and operating a mobile home park, according to the court in *Davis v. Davis*, 864 So. 2d 458 (Fla. 1st DCA 2003). Inside city limits, an unlimited value can be protected for up to one-half acre, but the use has to be purely as a homestead.

Homestead creditor protection is not necessarily limited to estates held in fee simple. Some Florida courts have found that homestead creditor protection can be extended to include long-term leasehold interests. For example, in *Geraci v. Sunstar EMS*, WL 2012 WL 2401793 (Fla. 2d DCA June 27, 2012), the court determined that a 100 year lease entered into in 1976 qualified for creditor protection in 2012. Stating that any beneficial interest in land may entitle its owner to the exemption, the court directed that the proper inquiry to determine whether a property qualifies for protection is whether: 1) the debtor intended to make the property his or her homestead; and 2) whether the debtor used the property as his or her primary residence. Unfortunately, not all Florida court decisions support the position that long-term leasehold interests qualify for creditor protection, and there is no guarantee that a debtor will be successful when claiming the homestead exemption for a long-term leasehold interest.

Homestead Protection Even Trumps the Florida Fraudulent Transfer Statute

In 2011, the Florida Supreme Court ruled in *Havoco of America, Ltd. v. Hill*, 790 So. 2d 1018 (Fla. 2001) that the constitutional homestead protection laws trump the statutory fraudulent transfer rules, so a person can intentionally defeat creditors by putting assets into a homestead or paying off a homestead mortgage immediately before or after a judgement is entered.

The remaining risk for Florida homeowners is that if three creditors can force the homestead owner into bankruptcy, the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act provides a 1,215 day ownership requirement, a 720 day residency requirement, and a possible 10-year fraudulent transfer look-back period.

In addition to homestead protection, married couples can own their homesteads as tenants by the entireties, which prevents the creditors of one spouse from penetrating the joint ownership, unless the creditors have a judgement against both spouses. In such circumstances, the protection offered for homestead need not be used, so the Bankruptcy Act exception described above will not apply and the debtor spouse can file bankruptcy and keep the entire homestead, assuming that a fraudulent transfer of the homestead into tenancy by the entireties has not occurred within four (4) years before the bankruptcy filing.

Homestead Disposition Prohibitions Surprise Many

It is especially important to note that the Florida Constitution prohibits an individual owner of homestead property from transferring or devising (during his or her lifetime or upon death) the property without consent of a spouse, and if the owner of homestead property dies with a minor child the disposition of the homestead under any Will or Trust will be ignored! If the homestead owner is married the spouse will receive a life estate or may elect to have a 50% ownership interest and the children will receive a vested remainder interest or a 50% co-tenancy interest if the surviving spouse elects to receive 50% co-ownership. If there is no surviving spouse then the children inherit directly. If there is a minor child there is no way for the homestead owner to have the property pass into Trusts for the descendants.

These rules and solutions for the problems they present will be explained in depth in Part II of this Article.

Tenancy by the Entireties

The Florida law of tenancy by the entireties can be quite tricky, and a great many married couples assume that all of their joint assets are protected from the creditors of one spouse, without realizing that what they actually own is a joint tenancy with a right of survivorship that does not satisfy all six of the unities required for tenancy by the entireties.

Of particular concern will be brokerage and bank accounts where the couple checked the joint with right of survivorship box instead of the tenancy by the entireties box when opening the account. When this occurs, it is not possible to change the account agreement, and a new account needs to be opened and will receive the assets from the prior account.

A good many other issues can apply when married couples attempt to own their assets as tenants by the entireties, and oftentimes a family limited partnership or family LLC will be established to be owned primarily by the husband and wife as tenants by the entireties in order to protect underlying assets using both tenancy by the entireties and charging order laws (which are mentioned below) at the same time.

Where one spouse lives in Florida and another spouse lives in one of the other states that recognize tenancy by the entireties property, the creditor protection will most likely apply for the

Florida resident spouse. The treatment of the other spouse will be subject to the law of where the other spouse resides.

Married couples living in northern states who own property in Florida may also claim the tenancy by the entireties creditor immunity, which has been held to apply for real estate and may also apply for intangibles such as bank and brokerage accounts. In the case of *In re Cauley*, the Bankruptcy Court for the Middle District of Florida in 2007, allowed non-Florida residents to protect real estate located in Florida held as tenancy by the entireties from bankruptcy creditors, despite the fact that the property was not considered to be their homestead. While non-Florida residents are not afforded homestead protections, tenancy by the entirety is created by common law and is not provided for in either statutes or the Florida Constitution. There is no case law that limits the protection of property held by tenancy by the entirety to Florida residents only, so according to *Cauley*, these protections apply to both residents and non-residents, and bankruptcy courts must apply the law of the state that is the situs of the debtor's real estate, so married couples living anywhere can apparently acquire Florida real estate as tenants by the entireties and protect it from the creditors of any one spouse!

Personal property held by tenants by the entirety is governed by the state of residence of the owners, and does not have the protection of Florida law if held in Florida. *See In re Estate of Siegel*, 350 So. 2d 89 (Fla. 4th DCA 1977).

The common law rules with respect to the elements required to qualify a property interest as tenancy by the entireties are reflected below, and were adopted from the English Common Law as it existed in 1776. The Florida Constitution specifically states that "The common and statute laws of England which are of a general and not a local nature, with the exception hereinafter mentioned, down to the 4th day of July, 1776, are declared to be of force in this state; provided, the said statutes and common law be not inconsistent with the Constitution and laws of the United States and the acts of the Legislature of this state." These elements have been applied by subsequent pronouncements of Florida courts occurring after 1868 when the Constitution was adopted.

To qualify property as tenants by the entireties, six unities must be satisfied. If any of these unities are not satisfied, then the joint asset will not be considered a tenancy by the entireties asset, and the consequent creditor protection from the creditors of any one spouse will not apply. These unities are as follows:

1. Unity of possession - both spouses have joint ownership and control - it may be acceptable that a deposit agreement allows either spouse to withdraw independently of the other on the theory that the power to withdraw is an expression of an authority of agency given by each spouse to the other.

2.Unity of interest - each spouse has the same interest in the account - it is not a problem if one spouse deposits all or most of the funds into the account as long as each spouse has the same interest immediately after the deposit.

3.Unity of time - the interests of both spouses in the asset must originate simultaneously in the same instrument, such as on the signature card. Do not try to convert an individual trust into a tenancy by the entireties trust. Instead, transfer assets from the individual trust to a new tenancy by the entireties trust.

4.Unity of title - both spouses must have ownership under the same title.

5.Survivorship - on the death of one spouse, the other spouse becomes the sole owner of the entireties property.

6.Unity of marriage - of course, the owners must be legally married under Florida law. Many clients become confused and believe that joint accounts with any third party or a significant other will be protected. Same sex marriages from other states will not be recognized by Florida Courts for purposes of this exemption. Florida Statute Section 741.212.

Assets held jointly before the marriage should be re-transferred from the spouses jointly to themselves as tenants by the entireties.

Note that in the case of *In Re Caliri,* U.S. Bankruptcy Court Middle District of Florida August 8, 2006, 347 B.R.778, joint accounts created before marriage were found not to qualify as tenancy by the entireties where the couple did not overtly transfer their interests to themselves as tenants by the entireties after the marriage.

It may be possible to place the beneficial ownership of a trust under a tenancy by the entireties owned LLC that may be disregarded for federal income tax purposes. Perhaps the client's will can state "I own an LLC jointly with my spouse and on the death of the survivor of us the ownership of that LLC shall be transferred to be held under the trust, and the trust shall be administered and distributed pursuant to its terms" (This may work but should be thought through carefully.)

Experts do not all agree on whether a tenancy by the entireties owned LLC can be disregarded as a "single member entity" for federal income tax purposes, but this should be the proper treatment in a non-community property state. For a more in-depth explanation of this issue, you can read BNA's U.S. Income Portfolio on Disregarded Entities by Howard Abrams, Fred Witt & Lisa Zarlenga (704-2nd).

Other Unlimited Creditor Exemptions

Florida also offers unlimited protection for properly situated annuity contracts, life insurance contracts, regular and Roth IRAs, 401k plans, other qualified pension plans, 529 Plans, wages of the head of household, and wage accounts (and the wages therein for up to 60 days after deposit) as well as tenancy by the entireties protection, which can apply to any kind of asset. These other unlimited creditor protections are described in more detail below.

None of the above exemptions are subject to any limitation on value, but every creditor exempt asset other than homestead is subject to Florida's four year fraudulent transfer statute, which is based upon the Uniform Fraudulent Transfer Act.

Wages of the head of household are protected from creditors, even for up to six months after they have been deposited in a bank account under Florida Statute 222.11, but for closely held businesses or professional practices, it can be difficult to satisfy the court imposed tests of whether wages actually constitute profits or distributions from a business. Properly drafted Employment Agreements and compliance with periodic wage provisions can be crucial.

Florida Statute Section 222.14 offers unlimited protection for the cash surrender values of life insurance policies and proceeds of annuity contracts. Under the Florida Supreme Court case of *Goldenberg v. Sawczak*, 791 So. 2d 1078 (Fla. 2001), the Court specifically held that this protection applied to moneys received from surrendering an annuity contract prior to maturity.

Florida Statute Section 222.13 also provides that whenever any person residing in Florida dies leaving insurance on his or her life, such insurance will inure exclusively to the benefit of the person for whose use and benefit such insurance is designated in the policy, and the proceeds will be exempt from the claims of creditors of the insured, unless the insurance policy or a valid assignment provides otherwise. Nevertheless, if the beneficiary of the life insurance resides outside of Florida, his or her creditors may access it depending upon state law where he or she resides, and life insurance payable to an estate or to a revocable trust that has legal obligations to pay creditors will not be protected. Also, life insurance not owned by the insured will not be protected.

We encourage clients to have the beneficiary of life insurance policies be irrevocable trusts for specified individuals to protect against the creditors of those individuals.

Unemployment compensation benefits as defined in Fla. Stat. § 433.051(2) are exempt from all claims of creditors, as are disability payments (including lump sum proceeds from a settlement) under Fla. Stat. 222.18.

Pensions, IRAs, and other retirement accounts are protected from the creditors of any owner, participant or beneficiary, if the owner and the beneficiary live in Florida under Florida Statute Section 222.21. This statute was the subject of significant controversy in the past few years, as to whether a non-spouse beneficiary of an IRA or pension account who resides in Florida would have the benefit received exposed to his or her creditors. This was resolved by a 2011 revision in the statute, which specifically provides that the exemption applies to "an inherited individual retirement account."

Florida Prepaid Tuition Fund and 529 plans are not subject to attachment, garnishment or legal process pursuant to Fla. Stat. Section 222.22.

The statutory creditor exemptions extend after death to a debtor's probate estate, pursuant to Florida Statute Section 732.402. "If a decedent was domiciled in this state at the time of death, the surviving spouse, or, if there is no surviving spouse, the children of the decedent shall have the right to a share of the estate...”

Private Annuity Planning

Grantor Retained Annuity Trusts are trusts created by a grantor who contributes assets to the trust and retains a right to receive payment from the trust for a retained term. Private annuities paid under a private annuity arrangement (such as a GRAT or where assets are sold to a trust in exchange for a lifetime annuity payment right) should be a protected annuity contract under Florida Statute Section 222.14, if properly drafted as an “Annuity Agreement.” In *In re Mart*, 88 B.R. 436 (Bankr. S.D. Fla. 1988), the bankruptcy court sitting in Miami found that payments received under a private annuity agreement established between a grantor and a trust that he funded were exempt from creditors under the Florida creditor exemption annuity statute. This decision has been discussed by two Florida Bar Journal articles which debate the issue: "*Unraveling the Mysteries of the Florida Exemptions for Life Insurance and Annuity Contracts, Part 1*," written by Jonathan E. Gopman, Matthew N. Turko, and Howard M Hujsa and “*Creditor Rights Under Private Annuities and Grantor-Retained Annuity Trusts in Florida*,” by Alan S. Gassman, David L. Koche, and Michael C. Markham. The second article reviews the Florida law of creditor access to irrevocable trusts, and suggests language that can be used to help confirm that an annuity payment right qualifies as a creditor exempt “annuity contract” under the statute.

Protecting Qualified Personal Residence Trust Rights

Many taxpayers establish Qualified Personal Residence Trusts (QPRTs) to exclude their homes from federal estate tax. With real estate values solidifying and the excess supply of vacant homes and condominiums decreasing in Florida, QPRT’s remain popular.

QPRT terms provide that the Grantor will continue to have the right to use and occupy the residence for a term of years specified in the trust agreement. Once the possessory term has passed, the trust typically provides that ownership of the residence will remain in the trust and will be divided among beneficiaries after the death of the survivor of the Grantor and the Grantor’s spouse.

It would seem that creditors of a Grantor could usurp the possessory rights during the retained interest term, but one solution to this would be for the QPRT to sell the home and convert to an annuity payment trust since Treasury Regulation Section 25.2702-5(c)(8) requires the QPRT to specify that within thirty days of ceasing to qualify as a QPRT, the trustee must convert the assets to a separate trust that meets the requirements of a qualified annuity trust for the benefit of the Grantor. The only other alternative allowed under the regulations would be to distribute the assets to the Grantor, which opens them up to both creditor claims and estate taxes.

A properly drafted conversion annuity provision should qualify as a creditor exempt annuity under Florida Statute Section 222.14. This annuity would terminate at the end of the retained term, and the remaining proceeds would be transferred to the remainder beneficiaries of the trust.

Sample language that we have used in a QPRT to facilitate this process is as follows:

> If the Trust ceases to be a Qualified Personal Residence Trust with respect to certain property, such property shall, within thirty days, be held in a separate share and the interest of the Grantor shall be converted into a qualified annuity interest (as defined by Treas. Reg. § 25.2702-3 and the requirements for such interest shall be deemed incorporated into this Article) with the smallest fixed annuity payments permitted by Treas. Reg. § 25.2702-5(c)(8)(ii)(C) to be made to the Grantor each calendar month for the balance of the Retained Possession Term, provided that the Trustee is authorized to make the conversion at an earlier time. The commencement date of the qualified annuity interest shall be determined in accordance with Treas. Reg. § 25.2702-5(c)(8)(ii)(B), and the Trustee may defer and determine the payment of any annuity amount as provided in that Regulation. If the Trust ceases to be a Qualified Personal Residence Trust with respect to certain property, the intent of the Grantor is to provide for issuance of an annuity contract to the Grantor based on the terms of this Agreement.

A Look at 529 College Plans

Under Florida Statute Section 222.22, money paid into or out of, the income of, and the assets of any qualified tuition program are protected from the creditors of the account owner, contributor, or beneficiary. Additionally, the plan's earnings are not subject to federal income tax, so long as the earnings are used for qualified educational expenses, including tuition, fees, books, and room and board.

The state of Florida offers two types of 529 Plans: prepaid tuition and dorm plans, and savings plans. The Florida Prepaid College Plan is the largest prepaid program in the nation and offers various tuition fees and packages, including a dormitory option, which is not offered by many states. This plan allows you to prepay the cost of tuition, required fees, and dormitory housing so that your child's education costs will be paid for by the time he or she is ready for college.

529 Plans do not have to be owned individually. Clients who have investments held under family limited partnerships, LLCs, and/or irrevocable trusts for descendants can have these entities purchase 529 Plan investments to pay college-related expenses.

529 Plans also provide significant creditor protection. Under Florida Statute Section 222.22(1), money paid into or out of, the income of, and the assets of qualified tuition programs authorized by Section 529 of the Internal Revenue Code are protected from creditors of the plan's owner, contributor, or beneficiary. Some other states that provide creditor protection for qualified tuition programs include Colorado, Oklahoma, Oregon, Mississippi, and Kentucky.

These plans also offer significant tax benefits. The plan's earnings are not subject to federal income tax, so long as the earnings are used for qualified educational expenses, which can include tuition, required fees, books, supplies, and room and board. 529 Plans can be used to absorb otherwise taxable gains, to act as a tax shelter for the contributor, or as a vehicle for the gift tax annual exclusion when funding 529 plans for descendants. The author's 2010 Bloomberg BNA quarterly article, "Unconventional Uses of 529 Plans Should Not Be Ignored by Taxpayers and Their Advisors," provides further 529 Plan strategies.

Clients who have 529 Plans that are worth less than what they invested may find it advantageous to start new 529 Plans. The old 529 Plans can be viewed as a tax shelter for the client, and once it reaches the original investment amount, the client might want to cash it in without paying tax. The gain on the new plan will also not be subject to income tax. This principle is best illustrated by an example.

For example, John Smith opens a 529 Plan for his son and invests $50,000, which is now worth $30,000. If he simply waits until the Plan is worth $50,000 again and then his son spends these funds on college, there will be no income tax savings.

However, if he starts a new 529 Plan with $30,000 and then both 529 Plans grow to $50,000, he can use the newer one for college tax free, and can cash in the older one without paying taxes. This saves the taxes on $20,000 worth of growth that would have otherwise been taxable if the funds were not invested in a 529 Plan.

Charging Order Protection

Generally, a creditor who receives a charging order with respect to a member's (or partner's) interest in the entity does not have any authority to mandate distributions from the entity or to participate in the management and affairs of the entity.

While many advisors believe that the creditor holding a charging order can be taxed on income attributable to the member interest under partnership tax law, this is probably not the case. Louis Mezzullo's *Family Limited Partnerships and Limited Liability Companies* BNA Portfolio 812 correctly states as follows:

> While some commentators, relying on a revenue ruling dealing with an assignee of a partnership interest, believe a creditor with a charging order will be taxed on the income allocable to the interest subject to the order, it is more likely that the creditor will not suffer unfavorable tax consequences. Because any distributions from the entity to the creditor should be treated as a reduction in the amount owed to the creditor by the owner of the interest, under general tax principles the owner of the interest would recognize the income.

Florida Statute § 608.433 was amended in 2011 to provide charging order protection for multiple-member LCCs after the Florida Supreme Court got confused and surprised lawyers everywhere by concluding that the previous statute did not provide charging order protection. The revised Statute applies retroactively and specifically indicates that "a charging order is the **sole and exclusive remedy** by which a judgment creditor of a member or member's assignee may satisfy a judgment from the judgment debtor's interest in a limited liability company or rights to distributions from the limited liability company." The Statute also specifically provides for protection for multiple-member LLCs, stating that "in the case of a limited liability company having more than one member, the remedy of foreclosure on a judgment debtor's interest in such limited liability company or against rights to distribution from such limited liability company **is not available to a judgment creditor** attempting to satisfy the judgment and **may not be ordered by a court**."

It is unclear whether charging order protection is available for a multiple-member LLC when all of the member interests are subject to charging orders and/or pledges that make it unlikely or impossible for any member to expect to receive any distributions from the entity. Florida Statute Section 608.402(21) imposes a requirement that a "member" must have an "economic interest" in the LLC if the judgment exceeds what would reasonably expected to be derived from the member interest. If the judgment creditor could receive all expected future distributions from the LLC, it seems that the individual members may no longer have an "economic interest" in the LLC. Thus, it is possible that the individuals would no longer meet the statutory definition of a "member" and could lose charging order protection if there is no reasonable expectation of ever receiving a distribution from the entity.

Single-member LLC ownership offers no substantive protection from a charging order standpoint, but may help buy time where there is a judgment against the sole member. Under Florida Statute Section 608.433(6), a charging order is not the "sole and exclusive remedy" available to judgment creditors of a single-member LLC where the court of equity concludes that there are no other sources to satisfy the applicable judgment.

Many planners therefore advise clients who wish to use "single member LLCs" to have a separate member, which may be an irrevocable trust that is disregarded for income tax purposes so that the LLC can remain disregarded as well. Some planners have single member LLCs formed in Delaware, Nevada, or other states that have legislation that is favorable to single member LLC charging order protection, but there are no direct cases on point as to whether the law of another state can apply in a situation where the debtor and the use, possession and management of the underlying assets are situated in a state that does not offer single member LLC charging order protection.

UNAUTHORIZED PRACTICE OF LAW – CAN YOU ADVISE FLORIDIANS IN THE FIRST PLACE?

Florida Legal Practice Rule 4-5.5 permits a lawyer who is licensed outside of Florida to perform services that either (a) "arise out of or are reasonably related to the lawyer's practice in the jurisdiction in which the lawyer is admitted to practice" or (b) "are performed for a client who resides in or has an office in the jurisdiction in which the lawyer is authorized to practice" as long as the non-Florida lawyer does not (1) establish an office or other regular presence in Florida for the practice of law, (2) hold out to the public or otherwise represent that the lawyer is admitted to practice in Florida, or (3) appear in court or before an administrative agency unless authorized to do so by the applicable tribunal. This exception will not apply for a lawyer who has been suspended from practicing in any jurisdiction, or has been disciplined or held in contempt in Florida for any legal misconduct. Separate rules apply for lawyers admitted to practice only in jurisdictions outside of the United States.

In addition, a lawyer admitted and authorized to practice law in another state may provide legal services on a temporary basis in Florida if undertaken in association with a Florida admitted lawyer who actively participates in the matter.

It is safest to have a Florida lawyer actively involved to review documents and strategies in order to assure that the work is done properly. Malpractice liability insurance policies may also limit coverage for work done outside of the home state of a law firm having occasional Florida clients.

The Florida Supreme Court has shown that it will not be lenient on those who attempt to practice law here without a license. For example, Jay Mitton, an attorney who was not licensed to practice in Florida, and his company used to hold seminars on asset protection and estate planning in Florida. In 2000, the Florida Bar filed a complaint against Mitton, alleging that he was engaging in the unauthorized practice of law at these seminars. Mitton claims that he never practiced law in Florida, but was caught up in Florida's justifiable concern about non-Florida attorneys practicing law in the state without a license. The Florida Supreme Court entered an order permanently and perpetually enjoining Mr. Mitton and his asset protection company from practicing law in Florida. The Court's decision in this matter can be found at their website, www.floridasupremecourt.org, case number SC00-2171. Mr. Mitton's rebuttal to commentaries on this decision can be found at his Web site: http://jaymitton.com/floridarebuttal.html.

Specific questions regarding the practice of law in Florida by an attorney licensed in another jurisdiction may be answered by the Florida Bar by calling (850) 561-5840.

There has been a significant increase in the phenomenon of accountants forming companies and other entities for clients, and this is a violation of the unauthorized practice of law rules. Certified public accountants risk licensing sanctions or even loss of licensing for engaging in the unauthorized practice of law. Further, the vast majority of these accountants simply form the entity on the Secretary of State website and provide no documentation to confirm ownership, Operating Agreements or By-Laws, or to issue stock or partnership interests. This is an extremely dangerous practice, but the Florida Bar is apparently unwilling to take steps to prevent this significant risk of harm that can befall individuals or families who believe that they are receiving appropriate protection and tax characteristics that will simply not be the case upon IRS or Florida Department of Revenue audit or creditor challenge.

Part II of this Article will review a number of very important Florida laws, planning techniques, and traps for the unwary. This will include a review of the Florida Trust Code, creditor protection using Florida trusts, property insurance crisis information, Florida elective share, liability protection planning, and much more.

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