**Tax Section of the Florida Bar**

**White Paper on Proposed Revision to Fla. Stat. § 736.0505**

## I. BACKGROUND

This proposal originates from the Tax Section of the Florida Bar.

The proposed legislation amends Fla. Stat. § 736.0505 to provide enhanced estate planning and federal transfer tax planning opportunities for Florida residents through the use of a certain type of *inter vivos* irrevocable trust commonly referred to as a "Spousal Lifetime Access Trust" or "SLAT".

The Tax Cuts and Jobs Act (the "TCJA"), which took effect on January 1, 2018, substantially increased the combined estate and lifetime gift and generation skipping transfer (GST) tax exemption amounts (such exemption amounts shall be referred to herein as the "Exemption Amounts"). In 2021, the Exemption Amounts are a historically high $11.7 million per individual ($23.4 million per couple). The TCJA will sunset on December 31, 2025, if Congress takes no further action. On January 1, 2026, the Exemption Amounts will be reduced to approximately $6 million per individual (amounting to the $5 million Exemption Amounts from 2011 as adjusted for inflation).

Given the current economic environment and government spending related to the impact of COVID-19, including the largest economic relief bill in U.S. history known as the Coronavirus Aid, Relief, and Economic Security Act ("CARES ACT"), Congress will look for avenues to increase tax revenue. Upon sunset of the TCJA, the Exemption Amounts will be reduced by half, thus increasing tax revenues without passing new laws. Further, under proposals already introduced in Congress, the Exemption Amounts could be reduced drastically before 2026. Accordingly, Florida residents have a limited window of time to take advantage of the high Exemption Amounts before they disappear.

The proposed amendment to Fla. Stat. § 736.0505 will provide Florida residents greater opportunity and flexibility to use the high Exemption Amounts to transfer wealth through the use of a SLAT in a tax efficient manner while maintaining current family financial stability.

## II. CURRENT SITUATION

The SLAT has become an essential estate planning mechanism for married couples to transfer wealth while allowing families to mostly retain the benefits of the transferred assets. SLATs allow Florida residents to use some or all of their Exemption Amounts by having one spouse (the "donor-spouse") gift assets to an irrevocable trust under which the other spouse is a beneficiary (the "beneficiary-spouse"). The assets in the SLAT can then be used for the benefit of the beneficiary-spouse during the beneficiary-spouse's lifetime. Upon the beneficiary-spouse's death, the assets generally continue in trust for the named beneficiaries without incurring federal transfer tax, regardless of how much the trust assets have increased in value since the initial gift.

The SLAT essentially replicates and accelerates the implementation of trust structures used for the benefit of a surviving spouse often created upon the death of the first spouse. Using this now while both spouses remain alive allows for use of the current Exemption Amounts. Waiting to transfer an amount of property into a similar trust upon the death of the first spouse to die may risk losing the opportunity for the family to benefit from the present historically high Exemption Amounts.

A significant issue arises when the beneficiary-spouse of a SLAT predeceases the donor-spouse. Under current Florida law, if the donor-spouse becomes a beneficiary of the SLAT after the beneficiary-spouse dies, or if the beneficiary-spouse has the power to appoint trust assets in further trust for the benefit of the donor-spouse, then the trust assets may be available to the donor-spouse's creditors under Fla. Stat. § 736.0505(1)(b). Similarly, the transfer of assets to a SLAT in Florida may be an "incomplete gift" if the donor-spouse is a potential future beneficiary or if the beneficiary-spouse has a power to appoint trust assets to the donor-spouse.[1] If the donor-spouse is deemed under state law to have retained the right to the possession or enjoyment of the trust assets after the death of the beneficiary-spouse, the SLAT assets may be included in the donor-spouse's gross estate for federal estate tax purposes.[2] These issues limit the broader use and benefits of a SLAT for Florida residents. Importantly, Florida residents may be able to create a more flexible SLAT under the trust law of other states which do not have the same restrictions existing under current Florida law.

Fla. Stat. § 736.0505(1)(b) prevents the creation of a "self-settled spendthrift trust" in Florida. A self-settled spendthrift trust is created when an individual transfers all dominion and control over assets to a trustee of an irrevocable *inter vivos* trust under which the individual is also a potential beneficiary. This rule also may prevent the donor-spouse of a SLAT from potentially receiving any benefit from the SLAT in the event the beneficiary-spouse predeceases the donor-spouse.

In 2010, Fla. Stat. § 736.0505(3) became law. Fla. Stat. § 736.0505(3) specifically carves out exceptions to the application of Fla. Stat. § 736.0505(1)(b) for (i) lifetime irrevocable trusts described in Section 2523(e) of the Internal Revenue Code (life estate with power of appointment in the beneficiary-spouse or "life estate with POA" trust), and (ii) lifetime irrevocable trusts for which an election under Section 2523(f) (a "qualified terminable interest property" or "QTIP" trust) has been made. The exceptions are intended to parallel the effect of Treasury Regulation Section 25.2523(f)-1(f), Example 11, to assure that no portion of the trust principal will be included in the donor-spouse's estate since the property is deemed passing from the beneficiary-spouse's estate, rather than the donor-spouse, which removes the trust from the self-settled spendthrift trust doctrine as to the donor-spouse.

Both the life estate with POA trust and the QTIP trust created for the benefit of the beneficiary-spouse permit the donor-spouse to be a possible beneficiary of the trust after the death of the beneficiary-spouse. However, no gift tax exemption is used upon creation of either of these trusts, as federal law provides the donor with a gift tax marital deduction but then requires that the

[1] See Revenue Ruling 76-103.
[2] See Revenue Ruling 76-103; Section 2036 of the Internal Revenue Code.

assets in the trust be included in the beneficiary spouse's estate for estate tax purposes (thus subject to the application of the beneficiary-spouse' available estate tax exemption on the date of his or her death; such exemption also potentially reduced after expiration of the TCJA). If the donor-spouse is a beneficiary of the trust after the beneficiary-spouse's interest ends at death, it is not considered a self-settled spendthrift trust under Florida law as a result of application of Fla. Stat. §736.0505(3).

Under current Fla. Stat. § 736.0505(3), a donor-spouse who creates a lifetime trust for a beneficiary-spouse without using Exemption Amounts can later be a beneficiary of the same trust when the beneficiary-spouse dies. Conversely, under current Florida law, if the donor-spouse used Exemption Amounts when creating the lifetime trust, the adverse tax consequences resulting from the application of current Fla. Stat. § 736.0505(3) effectively inhibit a donor-spouse from being named as a future beneficiary of the lifetime trust after the beneficiary-spouse's death. This disparity in current Florida law results in tax and other inequities for families where one spouse chooses to use Exemption Amounts for a lifetime trust for the initial benefit of that donor's spouse.

Further, Florida residents are at a distinct disadvantage compared to residents of other states which have enacted laws permitting the donor-spouse to be a beneficiary of a lifetime trust created for the beneficiary-spouse after the death of the beneficiary-spouse. If a Florida resident desires to create a SLAT with an interest passing to the donor-spouse upon the beneficiary-spouse's death, the Florida resident is forced to create the SLAT in one of the other ten (10) jurisdictions that would allow for such retention[3], or jurisdictions which allow self-settled spendthrift or asset protection trusts[4]. The assets in the SLAT are therefore removed from Florida, to the detriment of Florida investment and banking firms.

## III. EFFECT OF PROPOSED CHANGES

The proposed amendment to Fla. Stat. § 736.0505(3) will allow Florida residents to use an *inter vivos* irrevocable trust as an efficient and flexible vehicle to transfer wealth for the benefit of the donor's spouse and other beneficiaries. Florida couples will be able to take full advantage of current Exemption Amounts and address other situations where a SLAT is desirable, while potentially having access to the trust assets upon the beneficiary-spouse's death. The proposed changes to Fla. Stat. § 736.0505(3) will provide Florida residents the same estate and gift tax planning opportunities already available to residents of more than twenty (20) other states. Finally, the proposed changes to Fla. Stat. § 736.0505(3) are consistent with the exceptions available in current Fla. Stat. § 736.0505(3), as it is currently written.

[3] *See* Ariz. Rev. Stat. §14-10505(E); Del. Code Ann. tit. 12, §3536(c); Ky. Rev. Stat. Ann. §386B.5-020(8)(a); Miss. Code Ann. §91-8-504(d); N.H. Rev. Stat. Ann. §564-B:5-505; N.C. Gen. Stat. §36C-5-505(c); S.D.C.L. §55-1-36; Tenn. Code Ann. §35-15-505(d),(h); Tex. Prop. Code §112.035(g); Wisc. Stat. Ann. §701.0505(2)(e).

[4] Alaska, Connecticut, Delaware, Hawaii, Indiana, Michigan, Missouri, Nevada, Ohio, Oklahoma, Rhode Island, Utah, Virginia, West Virginia and Wyoming.

## IV. FISCAL IMPACT ON STATE AND LOCAL GOVERNMENTS

This proposal does not have a fiscal impact on state or local governments. It should be revenue neutral.

## V. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR

This proposal does not have a direct economic impact on the private sector.

## VI. CONSTITUTIONAL ISSUES

This proposal does not appear to raise any constitutional issues.

## VII. OTHER INTERESTED PARTIES

Other groups that may have an interest in this legislative proposal include the Family Law Section of the Florida Bar, the Business Law Section of the Florida Bar, the Real Property, Probate, and Trust Law Section of the Florida Bar, and the Florida Bankers Association.