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What's New Under the Sun in Florida with Trusts

Legislative changes may impact estate planning for residents

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Key points

- Beginning in 2021, the Florida Trust Code began heating up with some legislative changes that impact estate planning for Florida residents
- This article discusses four changes that may provide planning opportunities for residents of Florida
- You should consult with your legal counsel and other advisors on how these legislative updates may impact your estate plan

It's commonly known that Florida is hot; the average high in Palm Beach in December is 78 degrees. Perhaps that's one of the main reasons Florida is also a "hot" destination for new residents. Between April 2020 and April 2021, Florida added approximately 330,000 new residents[1].

Balmy weather isn't the only advantage of living in Florida or relocating to the Sunshine State. Beginning in 2021, the Florida Trust Code started heating up with some legislative changes that impact estate planning for Florida residents, including existing, new, full-time, and part-time residents. This article addresses four changes to Florida's trust laws:

- **New Directed Trust Act.** Effective July 1, 2021, Florida enacted the Florida Uniform Directed Trust Act which defines the responsibilities (and exposure) of trust directors and directed trustees[2].
- **New Community Property Trust Act.** Effective July 1, 2021, Florida's Community Property Trust Act allows married couples to hold assets in a community property trust in order to achieve a full basis step-up for property held in the trust upon the death of a spouse[3].
- **Trusts can last longer.** Effective for interests in Florida trusts created on or after July 1, 2022, such interests must vest within 1,000 years of that interest's creation. Florida's perpetuities period was previously 360 years (for trusts created between July 2001 and June 2022)[4].
- **New SLAT provision.** Effective July 1, 2022, so-called "spousal lifetime access trusts" created under Florida law receive expanded creditor protection in certain limited circumstances[5].

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New Directed Trust Act

When it comes to trusts, there are often several "players" named in the document. Each player has its own role/job to do when it comes to administering the trust. In addition to naming a settlor (the person establishing the trust) and a trustee (the person or institution responsible for administering the trust), trusts often name "directors," "advisors," and/or "protectors" and grant said individuals (who are not the trustee) with certain power over some aspect of the trust administration (commonly control over the investments of a trust's assets, i.e., an "investment trustee" or "investment advisor"). While their titles may vary, the concept of a "directed trust" is the same—there is a division of authority between someone who is not serving as trustee of the trust and the trustee.

In response to uncertainty surrounding certain aspects of directed trusts, Florida enacted the Florida Uniform Directed Trust Act (FUDTA), which expands Florida's directed trust laws and more clearly defines the duties and liabilities of trust directors and directed trustees of Florida trusts. Although not defined in FUDTA, in general, practitioners agree that FUDTA is intended to cover individuals functioning as a "trust protector." In particular, the legislative commentary to FUDTA provides that: "This act applies to any arrangement that exhibits the functional features of a directed trust within the meaning of this act, even if the terms of the trust use other terminology, such as "trust protector," "trust advisor," or "administrative trustee."

The FUDTA is a comprehensive law with many details that are outside of the scope of this summary, however, two key points are addressed by the Act:

1. A Florida trust director (or as noted above a trust protector, advisor, administrative trustee, etc.) has the same duties and liabilities as a trustee and because they are considered fiduciaries under the Act, they can be sued like a trustee (and can also be exculpated from liability like a trustee).
2. A Florida directed trustee can be sued for doing what a trust director tells the directed trustee to do, however, under FUDTA, a directed trustee can only be sued for doing what he, she, it is directed to do only if doing so would constitute "willful misconduct." Therefore, a directed trustee in Florida is likely not liable if something goes wrong because the directed trustee complied with the directions of a trust director unless doing so amounts to "willful" or "intentional" misconduct.

The forecast: The FUDTA became effective as of July 1, 2021, however, it applies to the actions of any trust director, even for trusts created before the effective date. You and your advisors should review existing estate planning documents to confirm that fiduciary appointments meet with your goals and objectives. Individuals and corporate fiduciaries named in your documents as a trustee, trust protector, investment advisor, trust director (or other fiduciary) should confirm their willingness to serve based on the facts and circumstances of your estate plan and this new legislation.

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New Community Property Trust Act

There are two recognized property regimes for spouses in the United States—"separate property" and "community property." In separate property states, married couples can have spirited discussions about who owns what, i.e., "this is mine and that is yours." Forty-one states in the United States, including Florida, are "separate property" states; however, special rules usually apply to property divisions on divorce.

There are nine states, however, that have adopted a "community property" regime which views all property acquired (and income earned) during marriage as being owed one-half by each spouse regardless of how title to property is taken, i.e., "this is ours."

The separate or community property classification of a particular asset is determined at the time the asset is acquired in accordance with the laws of the state in which the couple was domiciled when acquired. An asset's original classification is generally thought to not be altered when the couple later moves to a different state—that is, the character of property generally follows the couple as they move from state to state.

Effective July 1, 2021, Florida's Community Property Trust Act (CPTA) allows married couples to hold assets in a community property trust (a CPT). Why would Florida spouses want to establish and fund a CPT? Well, a CPT potentially offers a federal tax benefit to couples who convert separate property to community property using a CPT—a "double basis step-up" in the property held in the CPT.

Because Florida is a separate property state, under the current federal income tax laws, upon the death of a spouse, a surviving spouse inherits the deceased spouse's one-half share of jointly owned property and receives a basis adjustment for only that one-half share of the property. However, by contrast, in a community property jurisdiction federal income tax laws dictate that upon the death of a spouse, the entire community property owned by a couple will generally receive a step-up in basis equal to the property's fair market value.

Individuals may be able to take advantage of this tax benefit by holding assets in a CPT, under which each spouse holds a one-half interest in the trust's assets and the trust assets receive community property treatment.

The requirements for a couple to establish a valid CPT are:

1. The trust must expressly state that it is a community property trust within the meaning of the CPTA;
2. The trust must have at least one trustee who is either a Florida resident or a banking institution authorized to conduct business in Florida;
3. The trust instrument must be signed by both settlor spouses;
4. The trust must contain express language, provided in the act, stating the potential consequences of establishing a community property trust; and
5. The settlor spouses must be the only qualified beneficiaries of the trust while both are living.

The forecast: A properly established CPT will classify property transferred to it as community property; however, you should consult with your legal counsel about some of the risks of creating a CPT. For example, it is unclear whether the Internal Revenue Service (IRS) will permit a full basis step-up for property in a trust that grants community property treatment to individuals who do not live in a community property state, like Florida. Additionally, spouses may be foregoing certain asset protection benefits afforded to property transferred to the trust that was previously held by the spouses as "tenants by the entireties." Further, it is unclear what impact transfers of property by spouses to a CPT will have on existing pre or post nuptial agreements.

Trusts can last longer in Florida

Some families in Florida may want to start planning their reunions in the year 3022. In May 2022, Florida amended its statutory rule against perpetuities period—the maximum permitted duration of a Florida trust—from 360 to 1,000 years. Under the new law, an interest in any trust created on or after July 1, 2022, must vest within 1,000 years of that interest's creation. Florida had previously extended its perpetuities period from 90 to 360 years, effective for trusts created between January 2001 and June 2022.

The forecast: The expansion of the perpetuities period in Florida is important for individuals and families in Florida who want to use trusts to pass generational wealth in an asset protected and tax-efficient manner, for as long as possible. Because state laws vary, you should consult with your attorneys on the application of your state's rule against perpetuities and how that period may impact your estate planning goals and objectives.

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New SLAT provision

Over the last few years, estate planners have been busy advising clients on how to effectively utilize their federal, estate, and generation-skipping transfer (GST) tax exemptions prior to 2026, when the current increased exemptions ($12.92 million per individual for 2023) are scheduled to be cut in half, unless reduced by legislation before 2026 (which has been recently proposed in Congress). One type of trust that estate planners have suggested to clients is known as a "spousal lifetime access trust" (SLAT).

In general, a SLAT is an irrevocable trust created by one spouse for the benefit of the other spouse (which can and often does also include other beneficiaries, such as descendants). One of the benefits of using a SLAT is that in addition to utilizing an individual's lifetime gift tax exemption, the SLAT can provide the settlor (the individual creating the trust—the "contributing spouse") with indirect access to the trust assets by virtue of distributions made to the beneficiary spouse during the marriage. However, for Florida residents desiring to create a SLAT, it was unclear how the contributing spouse could access the funds in the SLAT if the beneficiary spouse predeceased him or her.

Under Florida's recent legislation, Florida law now permits a contributing spouse who survives the beneficiary spouse to be a beneficiary of the SLAT following the beneficiary spouse's death. Currently, Florida law allows the creditors of the settlor of a trust to access the trust's assets if the settlor is a beneficiary of the trust, even if distributions to the settlor are limited to what is needed for the settlor's health, education, maintenance, and support (this is known as a self-settled trust and includes your typical revocable living trust). Accordingly, many Floridians have been using the laws of other jurisdictions, such as Delaware, Nevada, and South Dakota, that extend creditor protection over trust assets which can be distributed to a settlor of a trust who is also a beneficiary of the trust.

Florida's new law provides that if a contributing spouse who is a Florida resident establishes a SLAT under Florida law that complies with three requirements, the contributing spouse could potentially become a beneficiary after the death of the beneficiary spouse without exposing the trust assets to the claims of the settlor's creditors (with some exceptions).

The three requirements for a Florida SLAT are:

1. The settlor cannot be a beneficiary of the SLAT until after the death of the settlor's spouse for whom the SLAT was established;
2. The settlor's spouse for whom the SLAT was established must remain a beneficiary of the SLAT for such spouse's lifetime; and
3. Transfers to the trust by the settlor must be considered completed gifts under the Internal Revenue Code.

The forecast: While the new law allows for some creditor protection for Florida SLATs, there are planning limitations and tax risks that should be explored before setting up a Florida SLAT. For example, because the beneficiary spouse must remain a trust beneficiary of the SLAT until his or her death, planning in the event of a divorce is foreclosed. Further, it is not clear whether the IRS would consider a contributing spouse's interest in a SLAT after the death of the beneficiary spouse as a "reversionary interest" which would cause the assets of the SLAT to be pulled back into the contributing spouse's estate for estate tax purposes, thereby defeating the tax planning goals of using the SLAT in the first place. The amended law is effective for SLATs created on or after July 1, 2022.

The developments summarized in this article provide welcome updates to Florida's trust code and can serve to provide new estate planning opportunities to Florida residents. You should consult with your legal counsel and other advisors on how these legislative updates may impact your estate plan. Further, because the legislation in this area is relatively new, you should also consider speaking with your advisors about planning in other jurisdictions, like Delaware, where laws governing directed trustees and SLATs, for example, have been in place for longer and as such, have more history and interpretation by courts.

Sources:

1 Florida's Office of Economic & Demographic Research, Demographic Forecast, July 18, 2022, Demographic Estimating Conference Florida Demographic Forecast (state.fl.us).

2 Florida Statutes Sections 736.1401-736.1416.

3 Florida Statutes Sections 736.1501-736.1512; Internal Revenue Code Section 1014(b)(6).

4 Florida Statute Section 689.225(g).

5 Florida Statute Section 736.0505.

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