HB 1237 Sections 7 and 16

WHITE PAPER

PROPOSED AMENDMENTS TO §§ 732.401 and 744.444, FLA. STAT.

I. SUMMARY

The proposed changes are submitted to address problems that result from the forced descent of homestead pursuant to F.S. § 732.401, while preserving the underlying public policy of the Florida Constitution and the statute designed to protect surviving spouses and minor children. The restrictions on the devise of homestead, as well as the forced descent of homestead which is not validly devised or which cannot be devised, present practical difficulties for the very persons intended to benefit from the restrictions. F.S. § 732.401 provides that homestead which has not been devised in accordance with the constitutional restrictions descends to the surviving spouse for life, with a remainder interest to the lineal descendants then living, per stirpes. This creates a difficult situation when the surviving spouse has certain economic duties (such as property taxes, insurance, ordinary maintenance, and mortgage interest) which the surviving spouse cannot afford. The rights of the decedent's descendants are jeopardized when the property is not maintained, taxes are not paid, or the mortgage payments are not paid. Florida's laws relating to partition do not permit the holder of a life estate or the remainder beneficiaries to force the sale of the home.

The proposed changes to sections 732.401 of the Florida Statutes are intended to offer planning alternatives, reduce confusion in a difficult area of law, and provide an alternative form of ownership for a surviving spouse. The election would function similar to the elective share election (see s. 732.201) and would allow a surviving spouse to elect between a life estate interest or a tenancy in common interest in the homestead property. If a surviving spouse elected to take a tenancy in common interest in the property (as opposed to a life estate interest), either the descendants or the surviving spouse could then force a partition of the property. That remedy is not presently available under the current statutory scheme. While the restrictions on the devise of homestead are addressed in Article X, Section 4 of the Florida Constitution, the Florida Constitution does not address how devise restricted property descends upon the death of the owner. That matter is solely addressed by the Florida Statutes, specifically F.S. 732.401, and as a result, the proposed legislation will have no effect on the provisions of Article X, Section 4 of the Florida Constitution and will present no constitutional concerns.

II. CURRENT SITUATION

A. Section 732.401

Restrictions on the Devise of Homestead. The Florida Constitution provides for restrictions on the devise of homestead, designed to protect surviving spouses and minor children. Article X, section 4 provides:

> (c) The homestead shall not be subject to devise if the owner is survived by a spouse or minor child, except that the homestead may be devised to the owner's spouse if there be no minor child....

While the devise restrictions on the homestead property are contained in Article X, Section 4 of the Florida Constitution, the Florida Constitution does not address how that property descends upon the death of the owner of the homestead. The descent of devise restricted homestead property is controlled by F.S. 732.401. Specifically, if the owner of homestead real property attempts to devise homestead in a manner not permitted by the constitution, or fails to make a devise of the homestead, ownership descends as provided in section 732.401, Florida Statutes, which provides:

> ... the homestead shall descend in the same manner as other intestate property; but if the decedent is survived by a spouse and one or more descendants, the surviving spouse shall take a life estate in the homestead, with a vested remainder to the descendants in being at the time of the decedent's death per stirpes.

When homestead cannot be devised, or is improperly devised so the devise is ineffective, the surviving spouse takes a life estate with a vested remainder in the decedent's descendants, per stirpes. This arrangement can create great burdens on the surviving spouse and the lineal descendants regarding the expenses and upkeep of the property which can actually result in the life estate / remainder ownership becoming a burden on the very people the law is designed to protect. [1] It is important to note that while the restrictions on the devise of homestead are addressed in Article X, Section 4 of the Florida Constitution, the Florida Constitution does not

[1] Jeffrey A. Baskies, *The New Homestead Trap: Surviving Spouses are Trapped by Life Estates They No Longer Want or Can Afford*, 81 Fla. Bar J. 69 (June 2007).

address how devise restricted property descends upon the death of the owner. The provisions regarding how the homestead property descends are addressed solely in the Florida Statutes, specifically F.S. 732.401, and therefore, any proposed changes to how the devise restricted homestead property descends upon the death of the owner is properly within the purview of the legislature.

Allocation of Ownership Expenses. Expenses are allocated between the life tenant and the remaindermen under the Florida Uniform Principal and Income Act.[2] The spouse, as life tenant, is responsible for paying the interest portion of mortgage payments, property taxes, insurance, and ordinary repairs. The decedent's descendants, as the remaindermen, are responsible for paying the principal portion of the mortgage payments, and to make extraordinary repairs. This creates a difficult economic partnership, especially when the decedent's descendants are not children of the surviving spouse. Often the surviving spouse cannot afford the obligations of the life estate. Other times, the remainder beneficiaries cannot or will not make the principal payments due on the mortgage, or make extraordinary repairs on the property. While this allocation of expenses applies to other life estates and remainder interests created intentionally by deed, will, or trust. , the life estate and remainder interests created by section 732.401 are forced upon the spouse and descendants.

A Life Estate the Spouse Can't Afford. Because the surviving spouse only has a life estate, he or she has a duty to the remaindermen to maintain the property. If the surviving spouse cannot afford to do so, selling the home may be an option, but is possible only if the remaindermen agree. The sale, however, creates complex estate and gift tax issues affecting all parties involved. The remedy of a partition action under Chapter 64, Florida Statutes, is not available to force the sale of the property since the remaindermen (descendants) do not have a current possessory interest in the property.

Value of the Surviving Spouse's Life Estate. Even if all parties involved agree to sell the home, valuation of the interests of the life tenant and remaindermen is very difficult. The spouse generally thinks the life estate is worth a great deal, the remaindermen think the life estate is

[2] §§ 738.701-738.705; § 738.801, Fla. Stat. (2009).

worth little (since it could end at any moment), and the IRS, except in limited circumstances, will apply its actuarial tables which do not take into account other relevant circumstances.[3]

Gift Taxes Upon Sale of the Home. There may be federal gift tax consequences resulting from the sale of homestead real property when certain estate tax elections have been made. The spouse's life estate is eligible for the marital deduction against the estate tax which postpones the estate tax on the homestead property until the death of the surviving spouse.[4] If an election has been made to qualify the life estate for the marital deduction, the home is later sold and the proceeds are divided between the spouse and descendants, the spouse will be considered to have made a gift of the entire proceeds (less the value of what the spouse retained in the division of the sale proceeds). The only way to avoid this potential gift tax trap would be to put the entire proceeds in a trust meeting the requirements of Section 2056(b)(7) of the Internal Revenue Code,[5] an unsatisfactory result in most cases. If the marital deduction has not been claimed for the homestead property, there will still be gift tax ramifications to a sale of the homestead if the proceeds are split between the spouse and descendants other than pursuant to the IRS' actuarial tables.

Disclaimers When Homestead is Not Validly Devised. In the past, some practitioners have attempted to use disclaimers as a way to cure an invalid devise of homestead and avoid the application of section 732.401. In reviewing the effect of a spouse's disclaimer, circuit courts have reached conflicting results. This issue needs to be resolved.[6]

B. Section 744.444

Section 744.444 enumerates the powers that may be exercised by a guardian without obtaining a court order authorizing a specific power. The statute presently does not grant a guardian the authority to seek permission to make an election under section 732.401 for an incapacitated surviving spouse.

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[3] The IRS tables may not be used for a person suffering from a terminal illness with a 50% probability of dying within one year. Treas. Reg. s. 25.7520-3(b)(3).

[4] The qualified terminable interest property ("QTIP") election.

[5] The spouse would be entitled to all the income for life. The descendants would receive nothing until after the death of the spouse.

III. EFFECT OF PROPOSED CHANGES

A. Section 732.401

Subsection (1) – Election Between a Life Estate or a 50% Share. Subsection (1), as amended, would provide the surviving spouse with a choice upon the death of the first spouse. The spouse could accept the life estate currently provided under section 732.401(1) or elect to take an undivided one-half interest in the homestead, with the decedent's descendants receiving the other undivided one-half interest. This alternative creates a tenancy in common relationship between the spouse and the decedent's descendants. The law applicable to tenancy in common interests is clearer in the areas of valuation, allocation of ownership expenses, and division of sale proceeds. In addition, the surviving spouse could utilize the partition procedures under Chapter 64 which are not available to a life tenant. One half of the net proceeds of the partition action would be payable to the surviving spouse and the balance would be payable to the vested remaindermen.

The proposed change to subsection (1) would not jeopardize the marital deduction against estate taxes currently available for homestead property interests passing to the surviving spouse. A review of law from other jurisdictions suggests that the value of property received by the surviving spouse as a result of an election under state law should qualify for the marital deduction. The key is that the rights under the state law election must be contingent only upon the spouse's election, and not subject to a discretionary award by the court or the actions of third parties.[7] It is also important to note that Florida's homestead rights exist at the moment of the decedent's death. The purpose of creating an election by the spouse is to avoid jeopardizing the qualification of the present life estate in homestead for the marital deduction while providing an alternative form of ownership if the election is made. The spouse's election of the one-half tenant in common interest should qualify for the marital deduction as to the spouse's interest.[8]

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[6] *See* R. Craig Harrison, *Homestead – The Post-Death Spousal Disclaimer: A Cure for a Constitutionally Prohibited Devise?*, 70 Fla. Bar J. 42 (April 1996).

[7] Rev. Rul. 72-153, 1972-1 CB 309; *Miller v. U.S.*, 35 AFTR 2d 75-1571, 74-2 USTC 13039 (DC OH 1974); TAM 7511120080A, 1975 WL 38616 (Nov. 12, 1975); Rev. Rul. 76-166, 1976-1 CB 287.

[8] The spouse's life estate in homestead qualifies for the marital deduction for up to 100% of the value of the homestead.

The proposed election should not jeopardize any homestead-related property tax provisions as to the surviving spouse's interest. Florida Statutes section 193.155 provides that a change of ownership in homestead real property results in the reassessment of homestead property values to current just value as of January 1 in the year following the change of ownership. Section 193.155(c)(3) provides that there is no change of ownership when the change in ownership is by operation of law under section 732.4015. Under section 193.155(8) a homestead owner can apply the benefits of the Amendment 10 Cap to a new homestead. This would benefit the surviving spouse who elects an undivided one-half interest in the homestead, sells his or her interest, and then establishes a new homestead.

Subsection (2). Subsection (2) in the present statute would be moved and renumbered as subsection (5). The new subsection (2) describes who may make the election, when the election must be made, and the manner of making the election.

New subsection (2)(a) provides that the surviving spouse may make the election. When the election is made by the surviving spouse's guardian or attorney-in-fact, the election can be made only after the court finds that the election is necessary for the spouse's best interests, taking into account the surviving spouse's life expectancy. The proposed amendment is patterned after the elective share procedures found in section 732.2135, Florida Statutes.

New subsection (2)(b) addresses the time for making the election by the surviving spouse. Subsection (2)(b) provides that the election must be filed within six months of the decedent's death. The time for making the election is tolled when a guardian or attorney in fact petitions the court for approval to make the election, as provided in subsection (2)(d). Although the surviving spouse would have a short period of time to make the election, he or she would still benefit from the constitutional protections by receiving a life estate in the homestead if no election is made.

When the decedent's estate is required to file a federal estate tax return and pay estate tax (which is due within 9 months after the date of death), it is critical to know whether the homestead election has been made in advance of the due date for the filing of the return and payment of tax. The life estate provided to the surviving spouse under section 732.401 is eligible for the marital deduction to the extent of the full value of the property under Internal Revenue

Code section 2056. The election to take an undivided one-half interest would result in only the value of a ½ interest in the homestead being eligible for the marital deduction. Whether the spouse accepts a life estate or elects a ½ interest, persons other than the spouse could be affected significantly by the reduction in the estate tax marital deduction by the value of a ½ interest in the homestead.[9]

The time for making the homestead election differs from the provisions of Florida's elective share statute. Consideration was given to the distinctions between the two elections. The surviving spouse potentially takes nothing under the elective share statutes if the time requirements are not met. The proposed changes to the homestead statute, by contrast, still provide the surviving spouse with a life estate if no election is made so the underlying constitutional policy is preserved whether or not an election is made.

New subsection (2)(c) provides that the election is irrevocable. This avoids the potential title problems that would be created if the election were made and then withdrawn.

New subsection (2)(d) requires that the election be made within 30 days of the court order authorizing the election by a guardian or attorney in fact or within the time otherwise provided by law, whichever is later.

Subsection (2)(e) provides that the election may be made by recording a notice of the election in the public records for the county or counties in which the homestead is located. This allows the surviving spouse to exercise the election even if probate proceedings have not been initiated. The homestead election procedure differs from the elective share procedures which require a pending probate proceeding. The homestead election might not require a full probate proceeding because protected homestead is not considered an asset of the probate estate.[10] Similarly, the procedures for making a disclaimer under Chapter 739 account for situations where no active probate proceeding is pending by providing for delivery of the disclaimer to the person or entity having a specific relationship to the asset.[11]

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[9] Protected homestead property is exempt from estate tax apportionment under Florida Statutes section 733.817, so others pay the tax, if any.

[10] § 733.608, Fla. Stat. (2009).

[11] § 739.301, Fla. Stat., Fla. Stat. (2009).

Subsection (3) – Allocation of Ownership Expenses. The responsibility for expenses allocated to a life tenant differs from that of a tenant in common. The following chart illustrates differences in the usual allocation of ownership expenses under the two forms of ownership.[12]

	Life Tenant Obligations	Obligation as 50% Tenant in Common
Mortgage Principal:	None	50%
Mortgage Interest:	100%	50%
Property Taxes	100%	50%
Ordinary Maintenance	100%	50%
Long-term Maintenance	None	50%

The proposed change provides that while the surviving spouse holds a life estate, he or she is responsible for the costs of ownership normally allocated to a life tenant. Upon electing an undivided one-half interest as tenant in common, the ownership expenses would then shift accordingly, as of the date the election is filed. The change in the allocation of expenses should not jeopardize the marital deduction against estate taxes if the election is made. Of course, there is no change in allocation of expenses if no election is made.

B. Section 744.444

The proposed changes to section 732.401 provide that a guardian can only make the election for the surviving spouse to receive an undivided one-half interest in the homestead after the guardian petitions the court for authorization to make the election. The proposed change section 744.444 would coordinate the statute with the proposed changes to section 732.401 and would specifically provide the guardian the right to file a petition requesting that an election be made on behalf of the surviving spouse.

IV. FISCAL IMPACT ON STATE AND LOCAL GOVERNMENTS

The restrictions on the devise of homestead are found in Article X, section 4 of the Florida Constitution. The homestead ad valorem property tax exemption is found in Article VII,

[12] The chart is for illustration purposes only and the allocation of expenses can be adjusted by the specific facts of any given situation as provided by current law.

section 6, as implemented in chapter 193, Florida Statutes. The Florida Supreme Court, in *Snyder v. Davis*,[13] noted that there are three categories of homestead, each with distinct constitutional and statutory provisions: creditor protection, restrictions on devise, and exemption from ad valorem property taxes. As the proposed changes are only dealing with the restrictions on devise, the proposed changes will have no impact on ad valorem property taxes or the exemptions relating thereto. Accordingly, there will be no impact on state and local governments.

V. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR

None.

VI. CONSTITUTIONAL ISSUES

Article X, section 4 of the Florida Constitution prohibits the devise of homestead real property when the decedent is survived by a spouse or minor child, but permits a devise to the surviving spouse if the decedent is not survived by a minor child. The descent of homestead property which cannot be devised, or which is the subject of an invalid devise, is controlled by the Florida Statutes and is not addressed in the Florida Constitution. Accordingly, the proposed changes do not conflict with constitutional provisions and are consistent with the public policy underlying the constitutional restrictions on the devise of homestead.

VII. OTHER INTERESTED PARTIES

The title insurance companies will be interested in this matter as it will have some effect on the issuance of title insurance.

[13] 699 So. 2d 999 (Fla. 1997).