Estate planning for the Florida resident

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Key Private Bank has teamed with Robert Eardley and Edwin Morrow to provide you with this reference guide on Trust and Estate Planning.

More information on Trust and Estate Planning can be obtained through any of our Key Private Bank offices in Florida. Please feel free to call or visit us at:

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Key Private Bank provides access to the expertise and services to manage all of your financial needs. From investment management, financial planning and insurance management to tailored financing and estate planning, our professionals work together with Key specialists from various disciplines to help you make the most informed decisions based on integrated, expert advice.

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Robert H. Eardley is a Florida Bar Board Certified Wills, Trusts, and Estates specialist. He is the founding member of the Law Office of Robert H. Eardley, P.A.

Mr. Eardley received his law degree from the University of Kentucky College of Law and a Master of Laws (LL.M.) degree in Estate Planning from the University of Miami (Florida) School of Law. He also holds an AV® (preeminent) peer rating from LexisNexis, Inc. and has been designated a Florida Super Lawyer® by Thomson Reuters. Mr. Eardley's law practice is concentrated in the areas of estate planning, Florida tax residency planning, and probate and trust administration.

Mr. Eardley is a frequent lecturer and published author on various estate planning topics, including Florida residency planning and advanced estate planning techniques. Several of his recent articles include "Securing A Florida Tax Residency for the Seasonal Resident" ©2015 for *Lifestyles After 50 magazine,* "A Second Marriage Estate Plan: 'Inheritance Rights' for Spouse, Stepchildren" ©2013 for the *Naples Daily News,* "Review of 2012 Estate, Gift Tax Changes" ©2013 for the *Naples Daily News,* "Plan for End of Life as with Retirement" ©2012 for the *Naples Daily News*, and "My Old Kentucky Home or the Sunshine State? Residency and Estate Planning Issues of Kentucky 'Snowbirds' in Florida" ©2010 for the Kentucky Bar Association.

Mr. Eardley is an active member of a number of professional associations, including the Florida Bar, the Kentucky Bar, the Naples Estate Planning Council, and the Trusts and Estates Section of the Collier County Bar Association. Also, Mr. Eardley serves as a member of the Wills, Trusts, and Estates Board Certification Grade Review Panel for the Florida Bar.

Prior to commencing his law practice, Mr. Eardley was an active-duty Naval officer and served as an airborne intelligence officer assigned to a reconnaissance squadron based in Europe.

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Active outside of Key Private Bank, Mr. Morrow is the outgoing Chair of the Dayton Bar Association's Estate Planning, Trust and Probate Committee, a Certified Financial Planner, Registered Financial Consultant, and a Non-Public Arbitrator for the Financial Industry Regulatory Authority (FINRA).

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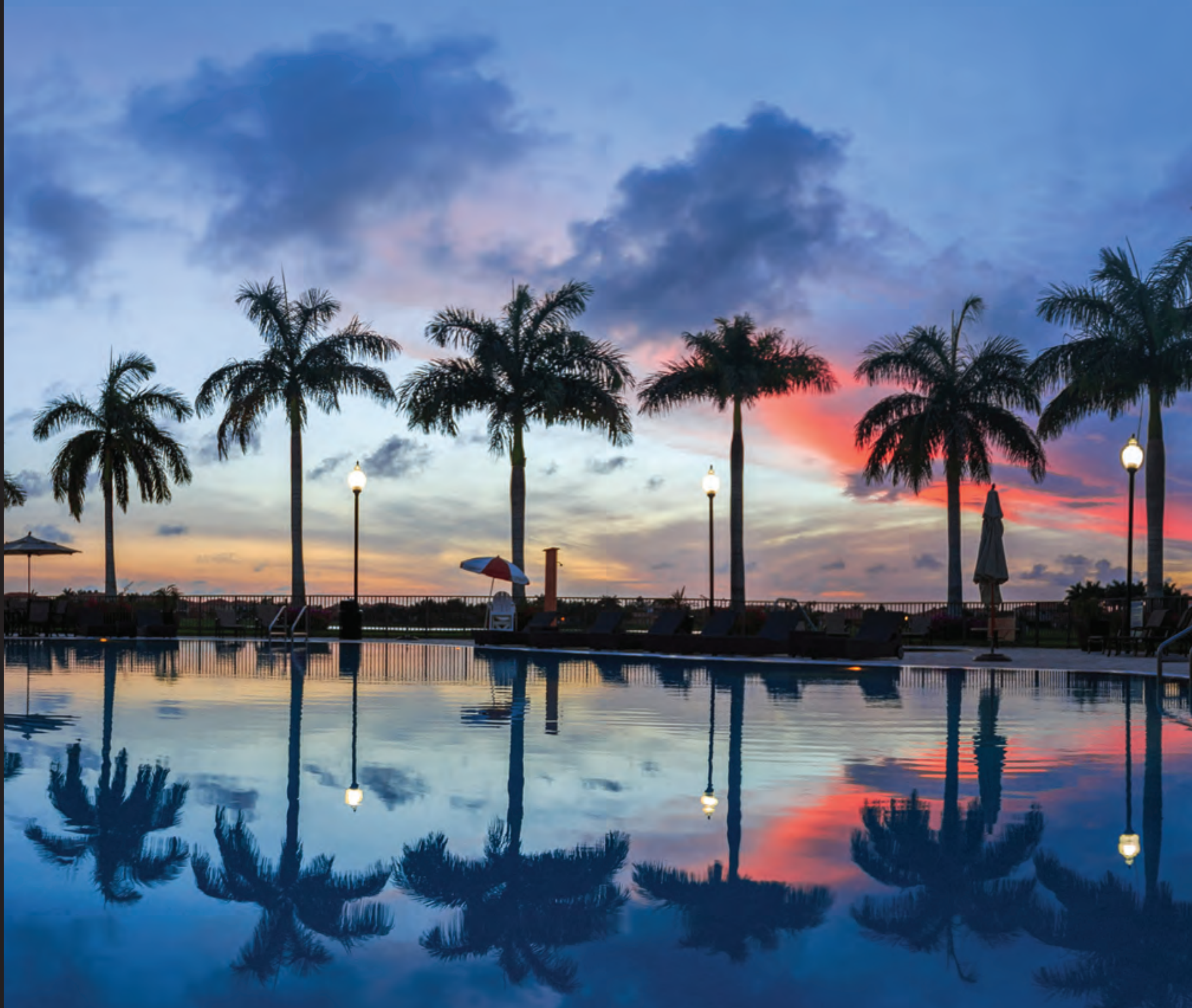
Introduction

Florida is well-known throughout the United States and the world as a popular tourist and retirement destination. Florida boasts a very mild climate, with only a slight difference between winter and summer temperatures, and coastlines with miles of beautiful beaches, keys, and islands, all with year-round water sports. Additionally, Florida has a number of popular tourist attractions, including Disney World and Busch Gardens, and is very taxpayer-friendly compared to most other states. For these reasons Florida is becoming increasingly popular as a home for people that used to live in other states or countries. However, perhaps the greatest factor attracting newcomers to Florida is the significant tax benefits for its residents. In fact, an average of nearly 400,000 people per year relocate to Florida and a handful of other states that have limited or no income or death taxation. This handbook will guide the Florida resident, or prospective resident, through many of the important estate planning steps to properly establish a Florida residency and implement an effective estate plan.



Article I

Advantages of Florida residency

No state income tax

First, and perhaps foremost, Florida is one of only seven states in the United States that impose no personal income tax – and it is the only "non-tax" state in the southeastern United States. The other non-tax states are Alaska, Nevada, South Dakota, Texas, Washington, and Wyoming.

Florida's no income tax policy is a long-standing part of state taxation philosophy – being first drafted into the State Constitution in 1885. Importantly, to remove Florida's Constitutional ban on a state income tax would require that a Constitutional amendment be enacted – a most unlikely event.

As noted, most states impose a state income tax, and this tax rate commonly is in the 6% to 8% range – or even higher. For example, the marginal state income tax rate for a New York resident is 8.82%, and for a Minnesota resident it is even higher – 9.85%. Therefore, by establishing a Florida residency one obtains an "automatic pay raise" merely by avoiding the state income tax from his or her state of origin.

Interestingly, Florida raises the majority of its revenue from the sales tax.

No municipal income tax

Also, the Florida Constitution generally bans municipalities from levying a personal income tax. However, many non-Florida cities do levy personal income taxes. For example, New York City residents are subject to a marginal city income tax rate of 3.40% in addition to state income tax.

Constitutional homestead property tax cap

Florida also has a long-standing public policy of providing homestead property tax relief stemming from the Great Depression era. For example, in 1934 the Florida Constitution was amended to provide a $5,000 exemption on the assessed value of one's homestead. This exemption, though not keeping pace with the cost of housing, now stands at $50,000.

However, the much more important property tax benefit given to Florida residents is the "Save Our Homes" homestead exemption provided in Article VII of the Florida Constitution. Under this exemption the assessed value of a Florida homestead for property tax purposes may only be increased in any year by the lesser of (i) 3% from the homestead's prior year tax assessment, or (ii) the percentage change in the consumer price index – notwithstanding the actual increase in the market value of the home.

This is not the case with a non-resident's property. The Florida home or vacation property of a non-resident may be adjusted annually by up to 10% of its prior year assessment. The result of this resident/non-resident disparity is that the Florida non-resident, over time, often pays thousands of dollars more in property taxes than the next door "Florida" neighbor with a comparable home.

With housing values still recovering from the large drop over the last decade, now is an opportune time to seek residency status and lock-in one's homestead Florida property tax assessment base. Of note, Florida residential real estate values increased by 11.3% in 2014 and are forecast to continue increasing throughout 2015.

No state death tax

Another significant tax benefit afforded to Florida residents is that it imposes no death tax (also sometimes referred to as an estate or inheritance tax, depending on the state). Years ago Florida enacted what is commonly referred to as a "pick-up tax," which dovetailed with federal estate tax law. The pick-up tax did not increase overall death taxes but merely redirected a portion of the federal estate tax collection to Florida coffers. However, several years ago Congress removed the state pick-up tax credit from the federal estate tax regime, and therefore Florida's pick-up tax essentially was revoked due to the federal change. Importantly, as of this writing, there appears to be no significant effort to implement a new Florida death tax system to replace the lost pick-up tax revenue.

No intangible personal property tax

Many states impose a tax on the "intangible" assets of its residents – typically assets such as brokerage accounts. Although Florida is known as a tax haven, for a number of years it did impose an annual intangible personal property tax (once at a rate of $2,000 in tax for every $1 million in value). Although this tax was modest in comparison to the income taxes of many other states, for years the intangibles tax was a hindrance to those considering Florida residency.

Fortunately for taxpayers, the intangibles tax was repealed more than a decade ago – and thus one of the last vestiges of a Florida individual tax has taken the same course as Florida's income and death taxes.

Asset protection

Florida law is very favorable compared with most other states for those concerned with asset protection. Thus, for risk-averse individuals, such as doctors and business entrepreneurs, Florida law provides a favorable environment in which to conduct business with reduced concerns for asset protection from a lawsuit.

Florida Homestead Protection During Life.

Florida homestead law is unique compared to most states. In short, the Florida Constitution provides that one's "homestead" is exempt from capture by the vast majority of creditors.

However, it is important to note that not all homes automatically qualify for homestead protection under the Constitution.

First, the owner's state of primary legal residence must be Florida and the Florida home must be the person's primary physical residence. Interestingly, Florida courts have ruled that not just the traditional Spanish-style villa or beachfront condo may be a homestead. For example, Florida courts have even granted homestead status to houseboats and motor homes. However, homestead status is not available if a business entity, such as a family partnership or corporation, owns the property.

Second, the Constitutional protection is limited to one-half acre if the home is located within a municipality, or to 160 acres if the home is located outside a municipality. Property exceeding the stated parameters generally is unprotected.

Third, if the owner is in bankruptcy, the owner must have resided in the Florida homestead long enough (generally up to 1,215 days) to be eligible for the maximum creditor protected status under the 2005 Federal Bankruptcy Act. However, if the homestead is owned jointly by spouses, a different category of protection is available regardless of the waiting period. Such joint ownership protection is discussed below in more detail.

Also, homestead protection is not just for United States citizens, but is available to any person whose primary residence is in Florida. Thus, risk-wary individuals from Europe and elsewhere can avail themselves of Florida's generous homestead creditor protection.

Florida homestead protection after death.

Florida homestead protection from the owner's creditors often continues after the owner's death. Specifically, the Florida Constitution provides that the benefit of creditor protection passes to one's relatives if they are the beneficiaries of the homestead. The upshot of this benefit is that the creditor of a decedent cannot collect a debt (or foreclose) against the decedent's homestead – unless the debt is secured by a mortgage on the homestead. Particularly, if there are insufficient funds in the estate to pay a debt, then the creditor goes unpaid and the relatives keep the homestead. And Florida Courts have broadly interpreted the term "relatives" to include not only one's spouse, children and grandchildren, but also cousins several degrees removed, nieces and nephews, and their descendants, and even more distant relatives.

Marital joint property.

Florida real estate, investment accounts, and private businesses (such as a limited liability company) jointly owned by spouses generally are presumed to be owned by the spouses in a marital status known as "tenants by the entireties." Importantly, Florida property which is owned in this status cannot be captured by the general creditors of just the husband or the wife. For creditors to capture the property, both the husband and the wife must be indebted to the creditor. Very importantly, this status even trumps creditor rights afforded by the 2005 Federal Bankruptcy Act. However, to obtain this protected status, it is highly advisable that all assets be clearly titled in both spouses' names followed by the terms "tenants by the entireties."

Article II

Establishing a Florida residency

Obtaining the various tax and other benefits by reason of Florida residency is fairly straightforward for a person whose only home is in Florida. However, the matter becomes complicated and calls for careful attention for a person who maintains a home in Florida and a summer residence elsewhere.

The primary concern for the individual in this situation is to take all steps possible to avoid any claim by the taxing authority in the state of origin that one's income and/or estate continue to remain subject to taxation in that state because of residency. More and more people are relocating from northern states, especially from those with high tax burdens, to Florida – with the result being the loss of significant tax revenue to those states. And this has not gone unnoticed by those states. In fact, the Wall Street Journal reported that Massachusetts has established a special "Domicile Unit" within its Department of Revenue to audit persons who claim non-residency but still maintain a significant connection to Massachusetts.

There are a number of recommendations that, in most cases, should be implemented to establish a Florida domicile and, with that, obtain the important tax benefits that accompany this status. However, it is imperative in each case that qualified legal counsel both in Florida and the state of origin be used to guide this process.

The words residence and domicile are both used above interchangeably. However, for legal purposes, the terms residence and domicile have very distinct meanings. Residence means a place where one possesses a dwelling. This can be, and often is, more than one place. Domicile, however, means the residence which is a person's primary home. And it is having a Florida "primary home" or domicile that triggers the various tax and other benefits.

Thus, when a person has one residence in Florida and another in the state or country of origin, it is critical to obtaining Florida's tax benefits that he or she establish the Florida residence as the domicile. However, because it is common to use the word residence but actually mean domicile, the remainder of this material will use the term residence or resident but only in the domicile sense.

Article III

A "checklist" to Florida residency

As a practical matter, Florida does not put obstacles in the way of a person desiring to become a Florida resident, provided he or she goes through the various governmental "hoops" to establish residency. However, for the person who will continue to maintain a seasonal residence in another state, the critical matter is to convince the taxing authorities of the other state that Florida is now the state of primary residence.

Having Florida as one's primary residence, for "northern" state tax purposes, is essentially a matter of qualifying as a non-resident of the northern state under that state's non-residency tax law.

Many northern states simply apply an annual "day-counting" test, with regard to the number of days a person spends in the northern state, to make the residency determination. However, even if the "day-counting" test is avoided, many states employ a back-up "residency intent" test that also must be avoided. And since the northern state cannot examine a person's mental intent for residency, objective factors are evaluated to determine the person's residency intent.

Along these lines, there are a number of steps to take that are useful for proving one's Florida residency intent. These steps, which are discussed below, are generally applicable to most states but are not exhaustive nor intended to substitute for tax counsel.

Step 1 – Obtain a Florida driver's license.

A person should obtain a Florida driver's license. Florida law currently requires that new residents obtain a driver's license within 30 days of establishing Florida residency. A driver's license can be obtained at any participating county government office.

Step 2 – Register to vote.

A person should register to vote in Florida and concurrently send a letter to the Supervisor of Elections in the former county of residence requesting removal from the election roster. For convenience, Florida allows a person obtaining a new driver's license to register to vote with the application for the new driver's license.

Step 3 – Apply for the Homestead Exemption.

If real estate is owned, a Homestead Exemption application should be filed with the county Property Appraiser's office. Interestingly, although the Homestead Exemption is necessary to obtain the "Save Our Homes" property tax cap discussed above, it is not determinative for homestead creditor protection. That is, one can fail to have filed for the Homestead Exemption but still potentially have the property considered homestead for creditor protection purposes.

To file a Homestead Exemption, all that is required is proof of one's ownership of a Florida residence (such as a Deed or tax bill), a Florida driver's license, a Florida automobile registration, a Florida voter registration card, and all applicants' social security numbers. To qualify for the Homestead Exemption for a particular year, all of the foregoing documents or instruments must be dated on or before December 31 of the prior year and filed by March 1 of the present year.

Additionally, if the residence is held in a trust, the Property Appraiser's office will require a copy of the trust and, if the "homesteader" is not a U.S. citizen, the person's green card is required.

As noted above, with a Homestead Exemption the 3% annual cap applies to property assessment increases and, as well, provides the owner a $50,000 reduction from the assessed taxable value of the homestead.

If the application deadline is missed, appeal can be made to the Value Adjustment Board, with just reason for failing to make a timely application for the Homestead Exemption.

Step 4 – File a Declaration of Domicile.

Another document that is important to file to demonstrate Florida residency intent is the Declaration of Domicile. This is an official government document by which the person states under oath that he or she is a primary resident of Florida and recites his or her Florida address. The Declaration is then recorded with the Clerk of Court for the county of residence. The original Declaration, upon recording with the county Clerk of Courts, is then returned to the applicant.

It is recommended that a copy of the filed Declaration of Domicile be sent to the taxing authority of the state of origin with a written explanation of the new residency status. This may be done concurrently with the taxpayer's filing of his or her final resident income tax return for the state of origin.

The main purpose of the Declaration of Domicile is to show one's current intent to be a Florida resident – especially from the perspective of a northern state tax auditor.

A Declaration of Domicile can be obtained on the websites of most counties or from the county Clerk of Courts.

Step 5 – Update the estate plan for compliance with Florida law.
Another important step to establishing Florida residency is to have one's estate planning documents updated for compliance with Florida law and to reflect Florida as the state of residence. Each state has unique rules pertaining to its estate planning documents (such as the Will, Trust or Power of Attorney), and these rules vary somewhat from state to state. Therefore, a person who intends to be a resident of Florida would naturally seek to have a valid Florida estate plan – particularly in the eyes of a northern state tax auditor.

Interestingly, a survey of the information available from a number of northern state tax revenue department websites reveals that these states often provide their auditors with a checklist to follow to determine if a person claiming to be a non-resident of the northern state should instead be considered a resident. Several of these checklists ask the troubling question "What county and state does the person's Will indicate he or she is a resident of?" This type of issue made the news headlines via the late Joan Rivers' Will, which reflected that New York law was to govern her Will (where she owned a Manhattan penthouse) but nevertheless stated that she intended to "reside indefinitely on a permanent basis" in California (where she lived in her daughter Melissa's home). Many observers believe this California reference was intended to posture the bulk of Ms. Rivers' $150 million estate to avoid New York's 16% death tax by locating her tax residency in California (which imposes no death tax).

In any event, regardless of any state tax avoidance concerns, it is important to have all estate planning documents made compliant with Florida law to ensure that one's testamentary wishes are carried out. For example, under Florida law the Executor of one's estate must be (i) a close relative or spouse of a close relative, (ii) a Florida resident or (iii) a Florida bank or trust company, such as KeyBank. Thus, a close and trusted family friend residing outside of Florida cannot be a Florida Executor. Many would not be aware of this issue unless Florida counsel was consulted.

Step 6 – Focus main activities and affiliations in Florida.
Additionally, it is prudent to restructure one's activities, relationships, and affairs to comport with a bona fide Florida residence. This would include spending a majority of one's time in Florida and relocating important relationships and matters, such as one's investment management firm, banking relationships, CPA, social and religious affiliations, safe deposit box, billing addresses, and heirlooms to Florida.

As noted above, some states have guidelines or checklists that direct a tax auditor to explore a number of these types of factors to determine where the taxpayer's "home" residence is. Thus, it is advisable to structure all of one's activities and affairs in a manner such that an independent observer would conclude that one's tax residency is in Florida.

Step 7 – Obtain a written, non-resident tax opinion from tax counsel in the state of origin.
Although many of the steps to securing a northern state non-residency status are similar from state to state, it is imperative for the person who will maintain a residence in a state that imposes an income and/or death tax to obtain a written tax opinion from a qualified tax attorney or CPA from that state. This opinion should identify what specific steps must be taken to be recognized as a non-resident by the taxing authorities of the state of origin. Each state has its own, unique tax residency rules and one's state of origin is not bound by a claim of Florida residency unless all applicable residency laws and regulations promulgated by the state of origin are avoided – and the only way to know these laws with certainty, and avoid them, is by use of qualified tax counsel from that state. The importance of obtaining northern state tax counsel was brought to the forefront in a recent decision from the Minnesota Supreme Court entitled *Kenneth B. Mauer v. Commissioner of Revenue*. In this case, native Minnesotan and NBA referee Ken Mauer purchased a residence in Ft. Myers in 2003, while still owning a residence in Minnesota, and then claimed he had switched to Florida residency for state tax purposes. Although Mr. Mauer did take some perfunctory steps to establish Florida residency – such as obtaining a driver's license and registering to vote – the Minnesota Department of Revenue disagreed with Mr. Mauer's Florida residency claim and assessed Minnesota resident income taxes. Ultimately the case went to the Minnesota Supreme Court and the decision of the Department of Revenue was upheld. Importantly, the Court applied Minnesota's 26-factor regulatory residency test and determined that Mr. Mauer's conduct simply was inadequate to relinquish his Minnesota residency.

Article IV

Florida estate planning issues

Estate planning often is subdivided into three parts. The first part is the implementation of legal documents to carry out the client's various testamentary wishes, such as who is to inherit estate property. The second part is saving estate taxes by utilizing appropriate estate planning techniques. And the third part is to ensure that the client's assets are postured so that each asset will actually pass at death in the manner that the client desires. In these respects, estate planning for the Florida resident does not vary significantly from that of residents of other states. However, Florida does have several legal peculiarities that must be addressed.

Estate planning documents

A complete Florida estate plan typically consists of at least three components: (i) a testamentary document (a Will and/or Trust), (ii) one or more Durable General Powers of Attorney, and (iii) an Advance Directive for health care. Many people have beneficiary designations for annuities, insurance, and retirement plans that also should be carefully considered in connection with their estate planning.

The Testamentary Document.

A "testamentary" document is the legal instrument used to identify the heirs of one's property and to designate who will have responsibility for handling all estate and legal affairs at death.

The Last Will and Testament.

For many decades the testamentary document of choice has been the Will – and the Will is still used frequently by Florida attorneys for smaller estates or for younger persons.

A common misconception is that a Will signed in a prior state is no longer valid once the person becomes a Florida resident. Fortunately, this is not the case. Under Florida Statute 732.502, a Will validly executed by a person in another state, while a resident of that state, remains valid in Florida after the person becomes a Florida resident.

However, it is important to note one critical caveat – even though the out-of-state Will itself is valid in Florida, this does not mean that all the terms of the Will are valid in Florida. This is discussed in more detail below. For this reason, among others, it is crucial that a new Florida resident have his or her Will updated for compliance with Florida law.

The Revocable or Living Trust.

In recent years the testamentary document of choice for many, in lieu of the Will, has been the Revocable or Living Trust (hereafter a Revocable Living Trust or an RLT). As with a Will, a Revocable Living Trust validly executed by a person in another state, while a resident of that state, remains valid in Florida after the person becomes a Florida resident. However, not all of the terms and provisions of the RLT may be valid under Florida law. This issue is discussed in more detail below.

Overview of the Revocable Living Trust.

A Revocable Living Trust is a common estate planning recommendation for a client (sometimes referred to as the "settlor" or the "grantor") who wishes to obtain important benefits that a Will cannot provide. From an estate planning standpoint, the RLT is also utilized in lieu of a Will to implement the client's testamentary wishes. During the past 20 to 30 years, RLTs have gained popularity as a sound device for accomplishing a number of legitimate estate planning goals.

Avoiding probate.

Probate is the court-supervised legal process of transferring a deceased person's property to his or her heirs. An RLT will avoid the costs and delays of a court probate at the client's death. The ability to avoid a court probate at death generally is the most valuable feature of an RLT.

Most people wish for their estates to avoid probate because this process can be relatively expensive, time-consuming, and inconvenient. Generally speaking, the probate process is expensive and prolonged due to the need for increased attorney involvement and by statutorily mandated probate procedures. Further, the probate process often produces a significant delay in the actual receipt of estate assets by the heirs. Also, if a person owns real estate outside of Florida, it is particularly important to transfer such real estate to the RLT to avoid a probate in that other state.

Mental incapacity.

An often overlooked benefit of the RLT is the ability to minimize the likelihood of a court-supervised guardianship in the event of mental incapacity. Upon the settlor becoming mentally incapacitated, his or her designee becomes the trustee of the RLT. Often the designee is a spouse or child of the settlor, or the settlor's bank or trust company, such as Key Private Bank. The settlor's chosen designee, as "successor trustee," then has authority to invest and manage the RLT assets according to the settlor's wishes as set forth in the RLT document. The RLT typically provides that the assets are to be prudently invested and paid out for the settlor's health care and support for the remainder of the settlor's life. Also, the settlor can choose more than one individual, or a trust company and an individual, as successor "co-trustees."

Parties to the Trust.

In the typical arrangement, the settlor who creates the RLT will also be named as the initial trustee of the RLT. He or she is often the sole beneficiary of the trust for life. Upon the settlor's death, the RLT then becomes irrevocable (like a Will), and the person or institution named in the RLT as the successor trustee becomes the acting trustee. Often a bank or corporate trust company, such as Key Private Bank, is named as the successor trustee to ensure that an orderly and professional trust administration is conducted.

As with a Will, the RLT provides for the disposition of the deceased's property at death to the intended heirs. The successor trustee is the party who is charged with the responsibility of distributing the trust property according to the terms of the RLT document.

Power to revoke or amend the RLT.

The typical RLT provides that during the settlor's lifetime he or she may amend or revoke the trust at any time and, as well, take possession of any trust property.

Funding the Trust.

For the RLT to be effective in avoiding probate, it is necessary that all property that otherwise would be subject to probate be legally re-titled into the RLT prior to death. Any property not transferred into the RLT before death generally will be subject to probate. Thus, a crucial element of implementing the RLT is the "follow through" work of funding the RLT once the trust document is executed.

Funding the RLT involves transferring legal title of assets from the settlor to the RLT. For example, if John Smith is funding his RLT, he will work with his investment firm to change the title of his accounts from his individual name to "John Smith, Trustee, John Smith Revocable Living Trust dated June 30, 2015."

Specific legal issues pertain to the transfer of certain types of property to the RLT, such as life insurance and homestead property, and therefore it is imperative to consult with a Florida attorney to develop an appropriate "funding plan" before actually transferring property to your trust.

Estate and income taxes.

A common misconception is than an RLT saves estate taxes. The RLT will not minimize estate taxes at death unless it contains appropriate tax reduction provisions. However, estate taxes can also be minimized by a properly drawn Will.

During the settlor's lifetime, an RLT does not produce any income tax consequences. For federal income tax purposes, the RLT is treated as if it did not exist. Instead, all income and loss of RLT assets is simply reported on the settlor's personal tax return. Also, any account opened for the RLT can utilize the settlor's social security number.

Asset protection.

Although many people believe that an RLT shields their assets from creditors, this is not correct. However, there are other trust and estate planning devices that can provide creditor protection.

Invalid provisions in a Florida resident's Will or Revocable Living Trust.

As noted above, although a Will or RLT made in another state remains valid in Florida once the person becomes a Florida resident, not all of the terms and provisions of the Will or RLT necessarily remain valid under Florida law. For this reason, it is critical that a new Florida resident promptly have his or her Will or RLT updated for compliance with Florida law. Some of the more common provisions at issue with a non-Florida Will or RLT are discussed below:

Executor Provisions. The Will is the document that, among other matters, nominates the Executor of one's estate. The Executor is the person or entity charged with collecting the deceased's property and distributing it in accordance with the terms of the Will. In Florida the technical designation for this role is the "Personal Representative." For many, the Personal Representative designation is one of the most important provisions of the Will.

However, Florida law limits who may be a Personal Representative to (i) a Florida resident, (ii) a close relative or spouse of a close relative, or (iii) a Florida bank or trust company, such as Key Private Bank. Stated another way, a friend who does not live in Florida cannot be the Personal Representative of a Florida estate. Thus, a person who relocates to Florida may bring with him or her a valid Will but an invalid Personal Representative designation.

Importantly, Key Private Bank is one of just a handful of Florida banks that has a primary emphasis on providing professional Personal Representative services to its clients as a cornerstone of its business history and model.

Penalty Provisions. In many states an “in terrorem” (from the Latin for “in fear”) or penalty clause may be inserted into a Will or RLT. This provision usually states that if a beneficiary attempts to challenge the Will or RLT, then that beneficiary will forfeit his or her inheritance. A penalty clause may be particularly important to a person who anticipates that strife will occur between heirs unless a significant price is to be paid by the contentious heir. However, under Florida Statutes a penalty clause is statutorily void, and thus such a provision in the Will or RLT of a Florida resident will not be recognized by a Court.

Guardianship Provisions. One’s Will also nominates the Guardian for any minor children. For many, the Guardianship provision is a very important part of the Will. However, Florida law limits who may be a Guardian for a minor child to either (i) a Florida resident or (ii) a close relative of the child. Unfortunately, this means that a close and trusted friend who does not live in Florida cannot serve as the Guardian for a Florida minor.

Homestead Issues. Florida law has traditionally been very protective of the homestead in a number of ways – and this protective inclination extends to the transfer of the homestead at death.

Once a person becomes a Florida resident, his or her home then becomes the homestead for testamentary purposes. And, interestingly, this is the case whether or not the person has actually filed for the homestead property tax exemption.

Under Florida law, if the homestead is not jointly owned by spouses with right of survivorship, then it only may be bequeathed outright to the surviving spouse. Any other bequest of the homestead is statutorily invalid. Also, if the deceased has one or more minor children, then even a bequest of the homestead to the surviving spouse is invalid. Instead, in both situations the ownership of the homestead, upon the death of the spouse who owns the homestead, is automatically divided, by statute, into a split ownership arrangement.

Specifically, when the spouse who is the home owner dies, the surviving spouse becomes the legal owner of a “life estate” in the home, but with the deceased spouse’s children entitled to possession and full ownership upon the surviving spouse’s later death. The “life estate” right permits the surviving spouse to use the home rent-free for the remainder of his or her life. Of note, the surviving spouse is not precluded from using the home as a rental property or from co-habiting there with others.

Alternatively, the surviving spouse instead may elect to take a 50% ownership interest in the home. In this case, the deceased spouse’s children become owners of the other 50%.

In any event, both the life estate and 50% ownership situations present unsettling difficulties. For example, upon a sale of the home, all owners (the surviving spouse and the deceased spouse’s children) must consent to the sale and, as well, all parties are entitled to a share of the proceeds.

Unfortunately, many individuals do not recognize the potential for this situation and the post-death split ownership arrangement is not an infrequent occurrence.

The author personally administered the estate of an elderly woman who settled in Florida with her husband of more than 50 years. They purchased a beautiful beachfront condo but retained their long-standing Massachusetts attorney to prepare their new Florida estate plan – even though they had become Florida residents. Upon the advice of the Massachusetts attorney, who was unaware of Florida’s unique homestead rule, the wife retained sole ownership of the beachfront condo until her death. As a result of his wife’s passing, the retired physician became the co-owner of the beachfront condo with his children. Not exactly the result the widower was seeking – and completely avoidable with proper planning.

Other Invalidity Issues. The above comments are not a comprehensive listing of all of the Will or RLT issues that must be considered upon establishing a Florida residency, but are merely a sampling of some of the more common ones that cross the desk of the Florida estate planning attorney. As with any matter of legal import, upon establishing a Florida residency the new resident should retain qualified Florida legal counsel to guide him or her in the process of implementing an appropriate Florida estate plan.

The Durable General Power of Attorney.

Having one or more Florida Durable General Powers of Attorney in effect is another crucial element of a complete Florida estate plan. A Power of Attorney instrument is a document by which one person (the “Principal”) appoints another person or entity (the “Attorney-in-Fact”) to act on his or her behalf.

The proper Power of Attorney instrument is “Durable”, which means that the authority granted to the Attorney-in-Fact remains in effect for the remainder of the Principal’s lifetime unless the Principal revokes it. Also, the Power of Attorney is statutorily suspended in certain situations, such as upon the initiation of a judicial proceeding to determine the Principal’s mental capacity.

Key Private Bank

Further, the appropriate type of Power of Attorney instrument is a “General” Power of Attorney. It is designated as such because it grants the Attorney-in-Fact the authority to act “generally” for the Principal.

Importantly, the Durable General Power of Attorney instrument is most useful for the Principal who is in his or her senior years and thus may not be able to properly attend to important financial matters, such as the payment of bills. With the Durable General Power of Attorney in hand, the Attorney-in-Fact can legally handle all such matters.

Customarily a Principal will appoint several Attorneys-in-Fact so that if one of the Attorneys-in-Fact dies or is otherwise unavailable, the other Attorney-in-Fact can assist the Principal. Most commonly, the Principal designates as Attorneys-in-Fact the Principal’s spouse, if any, and one or more adult children.

As noted above, many estate planning instruments prepared in other states remain valid after one relocates to Florida – due to Florida’s generous reciprocity statutes. However, many non-Florida Durable General Powers of Attorney cannot be fully utilized in Florida because of the special terminology and initialing requirements incorporated into Florida’s Durable General Power of Attorney code in 2011. Therefore, it is advisable that one’s Durable General Powers of Attorney be made compliant with Florida law upon moving to Florida.

The Advance Directive for Health Care.

Most states have enacted statutes pertaining to “end of life” health care decisions and the appointment of the persons who will make health care decisions for the ill person (referred to as the “Principal” under Florida Statutes). Often such written instruments are referred to generally by terms such as “Living Will,” “Health Care Surrogate” or “Health Care Power of Attorney.”

Florida Statutes provide that an “Advance Directive” is a written statement by the Principal, with proper witness and notary execution, which pertains to any aspect of the Principal’s health care. Florida Statutes further specify that a “Living Will” is a written statement, again with proper witness and notary execution, concerning “life-prolonging procedures.”

As part of a complete estate plan, a Florida resident is well-advised to implement a health care instrument compliant with Florida Statutes. In practice, many Florida attorneys draft the client’s Advance Directive and Living Will as a single document, since both documents intersect in important ways. Often such a document is styled as an “Advance Directive for Health Care,” or simply, an “Advance Directive.”

The Advance Directive addresses several critical matters. First, the Advance Directive directs who will make health care decisions for the Principal if the Principal becomes mentally incapacitated. This decision-maker is referred to in Florida Statutes as the health care “Surrogate.” Most commonly the Principal designates as Surrogate the Principal’s spouse, if any, and then one or more adult children as the alternate Surrogates.

Second, by the Advance Directive the Principal directs what is to be done if the Principal experiences a medical condition that requires “life-prolonging procedures” to continue his or her life – when the Principal is mentally incapacitated and in a condition from which recovery is medically improbable. Florida Statutes provide that “life-prolonging procedures” include life-support functions, such as artificial respiration and a feeding tube.

If one has not executed an Advance Directive, then the decision to continue or to remove life-support is held by the Principal’s statutorily-designated “proxy.” The general statutory sequence for the proxy appointment is first the spouse, then one’s adult children, then one’s parents, then one’s siblings, and finally a “close friend” (as determined in an affidavit from the close friend).

However, the statutory proxy (even if it is the spouse) may not have life-support removed unless it is shown by “clear and convincing evidence” – a very high evidentiary standard – that removal would have been the patient’s desire. Consequently, if there is any evidence that the patient desired life-support, then life-support may not be removed.

Further, if there is no evidence at all regarding the patient’s life-support desire, then life support may only be removed if removal is deemed to be in the patient’s “best interest.” Unfortunately, Florida statutes do not define what one’s best interest is – leaving open the possibility of another contentious “Schiavo” situation. For those old enough to remember, in 1990 Terri Schiavo (then 26 years old) inexplicably collapsed in her apartment and was subsequently diagnosed as being in a persistent vegetative state. Unfortunately, Mrs. Schiavo had no health-care documentation in place, and thus a tumultuous 15-year legal battle ensued between Mrs. Schiavo’s parents and her husband regarding her life-support situation. The legal battle ended in 2005 due to a court order directing that Mrs. Schiavo be disconnected from life support equipment.

Also, as with a Will or RLT, an Advance Directive executed by a person who was a resident of another state who later relocates to Florida remains valid in Florida. Nevertheless, it is advisable to prepare a new Advance Directive compliant with Florida Statutes upon relocating to Florida. The Florida Advance Directive Statutes utilize specific medical terminology which is unique to Florida, and thus it is prudent for the new Florida resident to have an Advance Directive that tracks the format and terminology to which the medical personnel in Florida are accustomed and understand.

Further, health care privacy rules were tightened a decade ago under the federal Health Insurance Portability and Accountability Act or "HIPAA." HIPAA provides stiff monetary fines and criminal penalties, including felony-level convictions, for the disclosure of patient medical information to a third party unless the patient has granted permission for the medical information to be released. A properly drawn Advance Directive will incorporate the HIPAA requirements and grant the Principal's health care Surrogate authority to access all medical information.

Spousal inheritance rights.

Most, if not all, states grant a surviving spouse the right to inherit a portion of the deceased spouse's estate regardless of the terms of the deceased spouse's Will or RLT – and Florida is no exception. Although such "spousal rights" are similar from state to state, Florida Statutes Chapter 732 provides a comprehensive and specific set of rules and benefits that apply with regard to a surviving spouse of a person who dies while a Florida resident. The philosophy undergirding spousal rights is that one spouse should not have the right to unilaterally disinherit his or her spouse – potentially leaving the surviving spouse penniless and a ward of the government. Nevertheless, a spouse may legally waive his or her rights by either a prenuptial or a postnuptial agreement.

Specific spousal inheritance rights.

Florida Statutes provide a surviving spouse two main rights. First, if the surviving spouse is not a joint owner of the homestead, then upon the death of the spouse who owns the homestead the property is automatically divided by Florida Statutes into a split ownership arrangement. Specifically, the surviving spouse becomes the legal owner of a "life estate" in the home, but with the deceased spouse's children entitled to possession and full ownership upon the surviving spouse's later death.

The "life estate" right permits the surviving spouse to use the home rent-free for the remainder of his or her life, subject to payment of the expenses and debts associated with the homestead. This life estate automatically passes to the surviving spouse if he or she is not designated in the estate plan as the sole beneficiary of the homestead. However, legal steps will eventually become necessary to demonstrate that the surviving spouse actually is the title owner of a life estate interest in the homestead – such as when there is a desire to sell the homestead.

Alternatively, the surviving spouse may elect a 50% ownership interest in the home. In this case, the deceased spouse's children become owners of the other 50%.

Second, a surviving spouse is entitled to an "Elective Share" of the deceased spouse's "Elective Estate." Although the assets which are included in the Elective Estate are delineated with great specificity under Florida Statutes Chapter 732, generally speaking the Elective Estate includes almost every asset that the deceased spouse owned (including RLT assets). This is in sharp contrast to some other states, such as Ohio, which grant spousal rights only over the probate estate. In any event, the surviving spouse is entitled to property equal in value to 30% of the Elective Estate – and this 30% share is designated as the "Elective Share."

To claim the Elective Share, the surviving spouse must affirmatively follow the required statutory procedure within a set timeframe. If not, then the Elective Share may be forfeited.

Of course, often the surviving spouse is a primary beneficiary of the deceased spouse's estate, and thus a surviving spouse's above interests become moot.

Waiver of spousal inheritance rights.

In second marriages it is not uncommon that each spouse has sufficient assets, independent of the other spouse, and desires that his or her entire estate to pass to his or her own children. Therefore, the spousal inheritance rights discussed above seemingly could circumvent each spouse's natural wishes. To accommodate such situations, Florida law permits persons, either before or after marriage, to waive some or all of their spousal inheritance rights.

The waiver of spousal inheritance rights before the marriage is implemented by a "premarital" agreement and the waiver of spousal rights after the persons have married is implemented by a "postmarital" agreement.

Although a complete discussion of such agreements is beyond the scope of this material, it is crucial to note that very strict rules apply with regard to the implementation of valid and enforceable premarital and postmarital agreements, and thus these agreements should only be entered into with the utilization of qualified Florida legal counsel.

Article V

The federal estate, gift, and generation skipping transfer taxes

The federal transfer tax system was changed dramatically in early 2013 when Congress enacted the American Taxpayer Relief Act (“ATRA”). Specifically, ATRA lowered the federal estate, gift, and generation-skipping transfer tax rates to 40% – from the high of 55% that had been in effect for decades – and set the base exemptions at $5 million apiece. ATRA also provided for annual inflation adjustments to each exemption ($5.43 million as of 2015). And, very importantly, ATRA made all of these benefits permanent.

Also, a very significant benefit for surviving spouses called the “Deceased Spousal Unused Exclusion Amount” (DSUE), or, more commonly, “portability,” was made permanent under ATRA.

The concept of portability is relatively simple: when one spouse dies, the surviving spouse may file a simplified federal estate tax return (no tax is due) and thereby transfer the deceased spouse’s remaining estate tax exemption, or DSUE, to the surviving spouse’s exemption on file with the IRS. While portability does have flaws, it largely corrects an injustice that otherwise occurs when the beneficiaries of a married couple, with no estate tax reduction planning in place, pay millions more in estate tax than the beneficiaries of a couple who die with such planning (typically a “Family Trust”).

However, using a “portability plan” to save estate taxes, in lieu of a Family Trust-based plan, is not without risks. For example, the survivor’s DSUE may be lost by an incorrect or late estate tax return filing, by an executor who declines to file the required return or by the survivor’s subsequent remarriage. Also, the generation-skipping transfer (“GST”) tax exemption cannot be transferred to the survivor. Further, using a Family Trust provides creditor protection, divorce protection, and income tax benefits for the spouse in addition to automatically capturing the deceased spouse’s exemption.

Further, it is recommended that those couples with estates under exemption should also re-examine their estate plans to consider optimizing such benefits, even though the federal estate tax is not a concern. For instance, a Family Trust may enable the surviving spouse to shift income tax liability, increase charitable tax deductions, and reduce income tax liability at the surviving spouse’s death.

Article VI

Planning techniques to reduce estate, gift, and GST taxes

Although the estate, gift, and GST taxes can produce enormous tax liability for larger estates, proper planning can serve to greatly reduce or eliminate these taxes as well as to postpone these tax liabilities. The following are some of the more common planning techniques available to achieve these goals.

Fully utilize the estate and GST tax exemptions

Although ATRA has brought many tax benefits, it remains important to consider capturing one’s maximum estate and GST tax exemptions. While this is not difficult for the single person, for a married couple it is important to capture both spouses’ estate exemptions and, if suitable, both of their GST exemptions.

Many “simple” Wills or RLTs for married couples provide that the estate of the spouse that dies first passes outright to the surviving spouse. Fortunately, no estate tax is imposed at that point regardless of how large the deceased spouse’s estate is (provided that the surviving spouse is a U.S. citizen) due to the unlimited marital deduction. However, such a simple plan may have the effect of accidently wasting the first-to-die spouse’s exemption if the DSUE amount is properly claimed on a timely filed estate tax return. Also, the simple plan cannot capture the first-to-die spouse’s GST tax exemption because this is not transferable under the DSUE regime.

To address the non-portability of the GST tax exemption under the DSUE system, an estate plan may be implemented which places the first-to-die spouse’s exemption amount, at death, in a trust (a “Family Trust”) for the benefit of the surviving spouse. If desired, the surviving spouse may be both the sole Trustee and the sole beneficiary of the trust, and the Family Trust can last for the remainder of that spouse’s life.

Importantly, the IRS does not count the assets in the Family Trust as being owned by the surviving spouse, for estate tax purposes, at his or her later death. The result is that the surviving spouse, in the eyes of the IRS, only owns one person’s estate (his or her own) at death. Also, because the Family Trust utilized the first-to-die spouse’s exemption, the trust assets (including all appreciation thereon) pass at the surviving spouse’s death completely free of any estate tax, to the couple’s children or other heirs.

Further, an "optimal basis increase" provision may be incorporated into the Family Trust. This provision enables appreciated assets in the Family Trust to receive a "step up in basis" at the surviving spouse's death. "Basis" denotes the value from which the IRS determines gain or loss (to impose income tax) upon the sale of an asset. The heir of a Family Trust asset – after the surviving spouse's death – typically takes the same basis that the first-to-die spouse had, and thus the heir may pay significant income tax upon a future sale of the asset. However, an "optimal basis increase" provision causes each appreciated asset in the Family Trust to receive a new basis equal to its fair market value at the surviving spouse's death.

Also, in lieu of the surviving spouse serving as the sole Trustee of the Family Trust, it is often advantageous to have a bank or trust company (often referred to as a "corporate fiduciary"), such as Key Private Bank, serve as co-Trustee with the surviving spouse, or, alternatively, as the sole Trustee. A corporate fiduciary provides a number of important services that may not be met by an individual Trustee. The corporate fiduciary, in addition to ensuring that all ongoing legal and tax matters are handled properly, such as the preparation and filing of the Family Trust's federal income tax returns and annual beneficiary accounting, also serves to ensure that the Family Trust assets are invested in accordance with accepted professional standards and that the distribution provisions set forth in the Trust are followed precisely and without partiality.

One common concern is that an elderly widow or widower, as a sole Trustee, may come under the influence of an outside party and either disburse Family Trust funds to that party or invest Family Trust funds with the outside party in an imprudent manner. Another common concern in a second marriage situation is that the surviving spouse may not invest or administer the Family Trust with sufficient impartiality for the deceased spouse's children. Such issues are eliminated when a corporate fiduciary serves as the sole or co-Trustee of the Family Trust.

In any event, the Family Trust is an important estate planning option for all married couples, regardless of whether or not the net worth exceeds the estate tax exemption.

Discounting techniques

To reduce one's estate tax liability, it is often desirable to utilize "discounted" assets. The "magic" of a discounted asset is that its value reported to the IRS legally must be its fair market value on the open market – but this value often does not represent its real value to the client. The discounted asset is then often used for intra-family gifts, to "superfund" a Family Trust, or simply to reduce the overall net worth at death.

Common examples of discounted assets are family limited partnerships (FLPs) and fractional (or percentage) interests in real estate. A fractional real estate posture, for example, would exist if a husband and wife each owned Florida real estate as separate (non-joint) 50% owners. Under the IRS's fair market value reporting requirement, a 50% separate interest in real estate is not reported at one-half of the full value of 100% of the property. This is because an independent buyer on the open market would pay less for a 50% interest since the buyer would have to share the property with a co-owner.

Fractional interest discounts.
Although fractional interest discounts vary to some degree, a conservative discount for real estate is 15% off full market value. Thus, assuming a couple's home is worth \$3 million (and disregarding any mortgages), by dividing the property between the husband and wife, as separate 50% owners, they automatically can reduce the value reportable to the IRS at death from \$3 million to approximately \$2.55 million – even though a post-death sale of the home would bring \$3 million.

FLP discounts.
A Family Limited Partnership (FLP) is a business entity created and owned by family members and typically holds marketable securities and real estate. The FLP often is recommended for its many benefits, such as a device for family members to consolidate assets for enhanced investment opportunities and to obtain asset protection. The FLP, if properly structured and administered, can also have the added benefit of being subject to IRS discounts of 40% or more.

An FLP is subject to discounting similar to that of fractionalized real estate, as discussed above, except that the discounts applicable to it are for (i) lack of marketability (since the FLP is not publicly traded on an exchange) and (ii) lack of control or "minority interest" (for the limited partnership portion, which typically is 99% of the ownership status). As with a fractional interest in real estate, an FLP also saves taxes, but to a heightened degree.

For example, assume that the Smith family creates an FLP and transfers \$5.05 million in marketable securities and real estate to the FLP in exchange for a 99% limited partnership interest for Mrs. Smith and with Smith adult children owning 1% as the general partners (via a corporate holding entity). Upon Mrs. Smith's death one would think that her 99% interest in the FLP would be reported and taxed at approximately \$5 million – the proportionate value of the underlying marketable securities. However, if a 40% discount is obtained, the value reported to the IRS would actually be \$3 million.

However, in recent years FLPs have come under increasing IRS scrutiny and, as of this writing, the Administration aspires to statutorily disallow all FLP discounts. Nevertheless, the FLP remains a very useful tax reduction option for large estates.

Discounting in light of the new $5 million exemption.
With the estate, gift, and GST taxes now affecting fewer taxpayers, existing discount structures should be re-examined. For larger estates still subject to these taxes, these discounts remain valuable – but each structure should be evaluated to ensure that it complies with IRS discounting standards. However, for estates below the exemption, discounting structures generally should be avoided because they no longer provide an estate tax benefit and may produce increased income tax liability. Although a detailed discussion of the income tax ramifications of owning a discount structure at death is beyond the scope of this material, anyone holding such a structure should promptly consult with his or her tax advisor.

Maximize low tax and leverage lifetime gifting techniques

In addition to the techniques discussed above, it is very important to consider transferring assets out of one's estate during life at either a no-tax cost or at a greatly reduced tax cost, and placing the assets in the hands of (or trusts for) the intended heirs. Such techniques serve as a supplement to the use of one's estate tax exemption via the Family Trust or the DSUE regime, discussed above.

The Zeroed-Out GRAT.
The Grantor Retained Annuity Trust (or "GRAT") is a trust arrangement sanctioned by the Internal Revenue Code and is an ideal "no-tax" cost gifting technique. Under the GRAT technique, a client transfers assets (usually a specific class of portfolio assets) into a GRAT and retains predetermined annual annuity payments from the GRAT for at least two years. Upon the expiration of the term of years, the balance (the remainder) of the GRAT assets passes to the client's beneficiaries or is placed in trust for them. The annuity payments back to the client are not considered gifts (since one cannot make gifts to himself or herself) and only the remainder component of the GRAT constitutes a gift reportable to the IRS. Importantly, however, the annuity payments are structured high enough such that the remainder component has a 0 value for gift tax purposes – hence the term "Zeroed-Out GRAT."

The GRAT is also subject to a beneficial tax loophole. Specifically, the client (as settlor of the GRAT) is legally obligated by federal income tax law to pay the GRAT's income tax liability, but such tax payments are not considered gifts to the GRAT. This loophole allows the GRAT assets to grow free of depletion by income taxes.

For the GRAT technique to prevail in transferring funds to one's heirs free of gift or estate tax consequences, it is only necessary that the total return on the GRAT assets during the retained term exceeds the IRS interest rate for the month the GRAT is created – and assets will remain in the GRAT upon the term expiration to pass to heirs free of gift or estate tax implications.

The GRAT is generally considered to be a "no-lose" technique. If the GRAT assets grow in excess of the IRS interest rate, then assets will pass to the heirs at the expiration of the set term and without tax liability. But if GRAT growth is sub-par, then all the GRAT assets return to the client via the annuity payments. In the sub-par scenario, the client winds up in the same position as if he or she had not implemented the GRAT.

For the highly motivated client, the Zeroed-Out GRAT technique can be enhanced by "re-gifting" each year's annuity payment back into a new Zeroed-Out GRAT and maintaining "rolling" annuity structure in place for the balance of the client's lifetime. Given enough time and positive investment returns, very significant sums can be removed tax-free from one's estate.

Example

Assume Dr. Baker, a 65-year-old retired physician, creates a $5 million Zeroed-Out GRAT for a 10-year term and the total investment return is 8% annually. Under the current applicable IRS interest rate of 2%, at the end of the GRAT term more than $5.1 million would remain in the GRAT to pass to his heirs free of gift or estate taxes. The annuity payments to Dr. Baker would be begin at $220,000 and increase by 20% annually (which is the maximum increase allow by the IRS). Further, the GRAT structure could obtain even more tax savings by using the rolling GRAT technique discussed above.

The Irrevocable Life Insurance Trust.

One tried and true estate tax savings technique is the Irrevocable Life Insurance Trust (ILIT). The ILIT is a trust arrangement that utilizes gifting to take assets out of one's estate and place the assets in an income- and estate-tax-free environment – the ILIT.

With this technique, the client creates an ILIT and transfers money to the Trustee of the ILIT. With the money the Trustee then purchases a life insurance policy on the client's life. The terms of the ILIT generally parallel the client's Will or RLT and often provide that, upon the client's death, the insurance proceeds are paid out to the client's heirs.

A significant advantage of the ILIT is that the insurance proceeds are not subject to estate tax in the client's estate. This is not the case with life insurance that is personally owned.

Also, life insurance proceeds – whether or not received by an ILIT – are *not* subject to income tax.

The ILIT technique, if contrasted with an IRA, demonstrates the ILIT's benefit. The IRA is subject to both estate and income tax – leaving perhaps as little as 30 cents on the dollar for the children after the client's death – while the insurance proceeds from the ILIT pass completely free of income and estate tax.

However, it is important to note that the transfer of funds into the ILIT to pay the premiums are considered gifts, subject to the federal gift tax system, and thus these gifts should be structured in a manner to capture as many $14,000 "Annual Exclusions" (discussed below) as possible, so that the client's exemption is not unnecessarily consumed.

Also, an existing life insurance policy may be gifted to an ILIT and enjoy the same benefits discussed above. Unfortunately, in this situation the IRS imposes a 3-year "look back" rule. Specifically, if the client dies within 3 years of transferring the policy to the ILIT, the policy proceeds will be included in the client's estate for estate tax purposes. However, this 3-year look back rule can be avoided with proper advance planning.

Qualified Personal Residence Trust.

Another useful estate tax savings technique is the Qualified Personal Residence Trust (QPRT). The QPRT is a trust arrangement authorized by IRS regulations that utilizes "leveraged" gifting. With this technique, the client transfers his primary home or vacation home to the QPRT and retains the right to reside at the home for a period of years set by the client, with ownership of the home generally passing to a trust for the spouse or children at the end of the set period.

Most gifts of property or money to a trust or to an individual are not "tax-efficient" – because the client's exemption will be reduced on a dollar-for-dollar basis by the value of the gift. However, under the QPRT technique, the reduction of the client's exemption is not the market value of the home (the dollar-for-dollar basis), as might be expected, but rather it is the market value of the home on the date of transfer to the QPRT minus the IRS stipulated value of the client's right to reside there for the set term of years. Thus, the QPRT only consumes a modest amount of the client's exemption (the value allocated to the children's future ownership component) but in reality passes a highly disproportionate value (the entire home) to the heirs when the QPRT term expires.

A downside to the QPRT is that the client must survive the term of the QPRT for the technique to work or the home must be transferred back to the client's estate and included in the estate for estate tax purposes. However, this is not necessarily a bad result because the client's estate remains in the same position had the QPRT not been created, and the IRS restores the exemption originally used by the QPRT.

Example

Mr. Jones, a 65-year-old retired executive, transfers his $1 million Florida home to a QPRT. Under the terms of the QPRT, he retains the right to reside at the home for 15 years. Assuming the applicable IRS rate at that time is 2%, this transaction consumes less than $460,000 of Mr. Jones's exemption but, upon the expiration of the 15-year term (assuming a 4% appreciation rate) his home will be worth more than $1.8 million and will pass to his heirs free and clear of further gift or estate tax implications.

This above example shows the power of the QPRT, using less than $460,000 in exemption to give away more than $1.8 million in value to one's heirs.

Tax-free gifts – the annual exclusion and "med/ed" exclusion

Although making a gift generally reduces one's exemption on a dollar-for-dollar basis, an important exception exists to this rule. Under section 2503(b) of the Internal Revenue Code, one can give away up to $14,000 per calendar year to as many individuals as desired without reducing one's exemption one bit. This provision is often referred to as the "Annual Exclusion", and the amount is indexed periodically for inflation in increments of $1,000.

For a senior client with numerous descendants, this special rule allows very significant value to be removed from the estate each year.

Example

Mrs. Miller is an 80-year-old widow with an $8 million estate and she is desirous of avoiding estate taxes. Also, she has 4 children, each of whom is happily married, and 12 grandchildren. In total, she has 20 potential beneficiaries, including the children's spouses.

Utilizing the Annual Exclusion, Mrs. Miller could give away $280,000 every year to her 20 beneficiaries without consuming any of her exemption. And given a decade of time, Mrs. Miller could entirely eliminate all estate tax liability.

However, if Mrs. Miller instead decides to retain these "giftable" funds until her death and then bequeaths the funds to her family, each bequeathed dollar (in excess of her exemption) would first incur a 40% estate tax before passing to the beneficiaries. This correlates to a $5,600 tax cost to retain each potential $14,000 gift until death.

In addition to the Annual Exclusion, unlimited funds may be paid directly to a health care provider or to an educational institution on behalf of another person pursuant to section 2503(e) of the Internal Revenue Code – often referred to as the "Med/Ed Exclusion" – and there is no limit on the amount that may be paid. Therefore, these Med/Ed gifts do not reduce one's exemption at all. However, such payments may be made to the educational institution only for tuition (room, board, books, etc., are excluded) or to the health care provider only for unreimbursed health care expenses. As well, there are other rules that apply in making such gifts, and thus legal counsel should be consulted prior to the initiation of any Med/Ed gifting plan.

Unfortunately, gifts to 529 Plans do not qualify for the Med/Ed exception.

Charitable giving and saving taxes

There are a variety of charitable giving techniques that can be of significant benefit, each with its particular benefits and drawbacks. The charitable options applicable to most clients are (i) the Charitable Remainder Trust (CRT), (ii) the Charitable Lead Trust (CLT), (iii) the Donor Advised Fund (DAF), (iv) the Private Foundation (PF), and (v) a direct gift to charity.

The Charitable Remainder Trust.
The CRT is a trust created either during lifetime or at death which ultimately passes assets to charity. Also, one can create a CRT for his or her own benefit or for the benefit of another.

Typically the CRT lasts either for a term of years or for the beneficiary's lifetime. During such time, the CRT pays the beneficiary (usually the client) either a set amount each year or, alternatively, a percentage of the CRT value. In either case, after the CRT period expires, the assets pass to the charity designated by the client.

A primary reason for the CRT's popularity is that it is tax-exempt and thus pays no income tax. Often a CRT is structured to be gifted a highly appreciated asset (such as stock) that, if sold by the client himself, would generate a large capital gains tax. If, however, the stock is given to the CRT and the CRT sells the stock, no tax is then due because the CRT is tax exempt. Instead, as the beneficiary receives payments from the CRT, the income earned by the CRT assets is allocated to the beneficiary's payments over the following years. The beneficiary then reports this income on his or her tax return. In short, the CRT has the effect of deferring capital gains taxation over many years while allowing the CRT assets to appreciate without depletion by income taxes.

Further, upon the contribution of assets to the CRT during life, the client is entitled to an immediate income tax deduction commensurate with the portion of the CRT that is deemed to be charitable in nature – usually 10% to 25% of the total CRT value.

The Charitable Lead Trust.
The CLT is essentially the inverse of the CRT and was made famous by being an integral part of Jacqueline Kennedy Onassis's estate plan.

Although there are a number of CLT variations, under the typical CLT technique the client creates a trust – the CLT – at death, and the charity of the client's choice receives the initial or front-end "lead" payments. Upon the expiration of the lead interest, the balance of the CLT property passes to the client's children or other heirs (or more likely, in trust).

The CLT technique is primarily used to reduce estate tax liability. In a typical scenario, a formula-calculated value of the estate sufficient to reduce the taxable portion of the estate to just under the taxable threshold – due to the estate tax charitable deduction (commensurate with the value of the charity's lead interest under IRS tables) – is bequeathed to the CLT. However, it is anticipated that over the term of the CLT the appreciation and income will be much greater than the actual required charitable payout – thereby leaving a large, but delayed, tax-free inheritance for the heirs when the CLT term expires.

The Donor Advised Fund.
The DAF is a tax-exempt charitable fund managed by a bank or investment company. Key Private Bank, for example, offers DAFs that can be coordinated with the management of one's non-charitable investment portfolio. Generally the client establishes a DAF account during life and, at death, a significant portion of the estate is bequeathed to the DAF. In creating the DAF account, the client customarily enters into a written agreement with the DAF manager as to (i) which charities the client desires to benefit and (ii) which family members are authorized to advise the DAF as to potential charitable recipients in future years. The DAF then pays out the client's funds to charitable recipients as the years go along. Importantly, assets bequeathed to the DAF qualify in full for the estate tax charitable deduction. To eliminate income taxes, it is common that the DAF is designated as the beneficiary of an IRA or qualified retirement plan rather than as a beneficiary of general estate assets.

A main benefit of the DAF is that there is minimal administrative or compliance work required by the client or the client's family (as compared to a Private Foundation) – and yet the designated family members nevertheless have the lead role in providing recommendations to the DAF manager as to which charities are to receive funds. Further, there is no cost to the client to create a DAF account.

The Private Foundation.
Like the DAF, the PF is also a tax-exempt entity. However, with the PF the client himself establishes it, either in the form of a trust or corporation, and then applies to the IRS for recognition of the PF as a tax-exempt entity. The client and the trustees or corporate officers of the PF, as the case may be, are responsible for the day-to-day administration of the PF, investment selection, tax compliance and reporting, and charitable beneficiary identification. Generally the PF is structured to be narrowly focused, such as scholarships to impoverished students attending a certain college. Upon the client's death it is common that additional estate assets are bequeathed to the PF.

A main benefit of the PF is that the client can be very specific as to his or her intended beneficiaries and can hand pick the trustees or corporate officers (often the client's children) who will carry out his or her intent. The main downsides to the PF are (i) the personal responsibility borne by the client and his or her children to carry out the various administrative responsibilities of the PF, (ii) a much larger proportion of the PF's assets are consumed by administrative expenses as compared to a DAF, (iii) the initial setup cost, and (iv) meeting the ongoing reporting and compliance requirements. Further, individuals giving to a PF are subject to less favorable income tax deductions as compared to a DAF.

Direct bequest to charity.
One very administratively practical charitable giving option is to bequeath assets directly to charity when both the client and the client's spouse are deceased. For example, one could make an IRA payable at death to the Red Cross, and these funds would pass directly into the Red Cross's general budget. Also, it is common that clients planning large value bequests enter into a written letter of understanding with the charity as to how the client expects the bequest to be administered. This is typical with bequests payable to universities, prominent charitable organizations and major hospitals – all of which have administrative officers to assist prospective donors in identifying the uses and purposes for the bequest. Also, the client may revoke a proposed charitable bequest at any time.

Tax benefits of combining IRAs with charitable planning.
Perhaps the highest tax-cost item to own, in terms of total potential tax liabilities, is a tax-deferred retirement plan such as an IRA, 401(k) or 403(b) (hereinafter each referred to generically as an IRA). It is not uncommon for the total post-death tax cost on an IRA to approach or exceed 70% due to the imposition of both the estate and income taxes. A similar consequence can occur with an annuity if a significant portion of its value consists of tax-deferred income.

Importantly, Roth IRAs are not subject to income tax but they are subject to the estate tax system.

For the client who has (i) potential significant estate tax exposure, and (ii) a bona fide and significant charitable intent, an ideal option is to utilize the IRA to fund charitable gifts after both the husband and wife are deceased. Charitable bequests structured in an appropriate manner qualify in full for both the estate and income tax charitable deductions. These deductions have the effect of giving 100 cents of every IRA dollar to the charity or charities, rather than the alternative of leaving as little as 30 cents or less of every IRA dollar to one's heirs.

Example

Dr. Williams is a 70-year-old retired engineering professor with no children. However, Dr. Williams wishes to leave enough money to his five favorite nieces and nephews so that they each will have a nest egg. Also, Dr. Williams has been a lifelong supporter of his alma mater, the University of Florida.

Dr. Williams' highest value asset is a $5 million IRA, and the value of his house and other assets is $5.43 million, for a total estate of $10.43 million.

Dr. Williams meets with his estate planning attorney, who determines that Dr. Williams has significant charitable intent and that $5.43 million (or $1.086 million apiece) is in line with Dr. Williams' desires for his five nieces and nephews. If Dr. Williams left both his estate property and the IRA to his nieces and nephews, as little as $3 million of the IRA may wind up in their hands, with the rest going to the IRS in the form of estate and income taxes. However, upon his attorney's advice, an estate plan is executed by Dr. Williams that leaves his non-IRA assets ($5.43 million total) to his nieces and nephews and designates the University of Florida School of Engineering as the beneficiary of his IRA at death.

In this case, Dr. Williams' new estate plan gives his nieces and nephews a $5.43 million inheritance and benefits his alma mater with a $5 million engineering scholarship fund – and eliminates all estate and income taxes.

Minimize inter-generational taxes with GST tax planning

The GST tax is a tax imposed on any gift or bequest to a relative who is 2 or more generations younger than the client or, in the case of a non-relative, is 37.5 or more years younger than the client. This younger beneficiary is referred to as a "Skip Person" by the IRS. The GST tax exemption for 2015 is $5.43 million and annually is adjusted for inflation in lockstep with the estate tax. Gifts or bequests to a Skip Person that exceed the exemption incur a GST tax of 40% in addition to any gift or estate tax. Therefore, clients usually do not give an amount in excess of their GST exemption to their grandchildren due to the draconian result of the GST tax. Nevertheless, GST planning opportunities are available to minimize the total death tax cost that a family would otherwise incur over multiple generations.

The primary opportunity in the GST tax planning arena is to create an estate plan that benefits one's children with an inheritance for life and then passes to the grandchildren – but avoids the estate and GST taxes at each child's death. Such a plan typically is referred to as a "generation-skipping trust" plan or a "Lifetime Trust" plan.

At the death of a single person, or the death of the survivor of a married couple, the estate will pay any estate tax owed and then, not uncommonly, will pass outright to the adult children. Although such a format is very simple, it may come at a huge tax cost if the estate tax will be paid a second time on the inheritance at each child's later death because the inheritance is then a part of the child's own estate.

This double tax concern can be mitigated or eliminated by the use of the Lifetime Trust plan. Under this plan, a child's inheritance is not given to him or her outright, but instead is placed in a Lifetime Trust for the child. Although the child will receive the economic benefit of the Trust, no estate or GST taxes are owed at the child's death to the extent that the parents' available GST exemption ($10.86 million for a married couple).

Example

Mr. and Mrs. Taylor are in their 70s and have a combined estate of $10.86 million. They also have two adult children in their 40s. Both children are successful professionals with large estates of their own. The Taylors know that with proper planning they can protect their entire estate from the estate tax when they are both gone by use of their separate $5.43 million exemptions. However, the Taylors know that their estate, once added to their children's personal estates, will be taxed at each child's death. The Taylors meet with their estate planning attorney, who advises them that their tax concerns at the child level can be eliminated by the use of a Lifetime Trust plan.

The attorney advises the Taylors that, under this plan, after they are deceased each of their children will receive a one-half share of their estate, or $5.43 million each, in trust for life – and that the Taylors combined GST tax exemption ($10.86 million) will be allocated 50% to each of those trusts.

The terms of the trusts provide that each child will be both the sole Trustee and the primary beneficiary of his or her trust. The attorney further advises the Taylors that each child is allowed to determine who will inherit their trusts at death – just as they would have been able to with an outright inheritance. And, even more, upon each child's death the child's trust, regardless of the amount of appreciation, will pass to the child's heirs free of estate and GST taxes. Their attorney advises them that IRS simply deems the trusts not to be part of the children's personal estates for tax purposes.

Also, in lieu of a child serving as the sole Trustee of his or her Lifetime Trust, it is often advantageous to have a corporate fiduciary, such as Key Private Bank, serve as a co-Trustee with the child, or, alternatively, as the sole Trustee. As noted above, a corporate fiduciary provides a number of important services that may not be achieved by an individual Trustee. For example, the corporate fiduciary ensures that all ongoing legal and tax matters of the Lifetime Trust are handled properly, such as the preparation and filing of the Lifetime Trust's federal income tax returns and annual beneficiary accounting. The corporate fiduciary also serves to ensure that the Lifetime Trust assets are invested in accordance with accepted professional standards and that the distribution provisions set forth in the Trust are followed.

Also, a corporate Trustee is the appropriate choice in a number of particular situations, such as for the child who (i) has substance abuse problems, (ii) is mentally impaired, (iii) is susceptible to undue influence or (iv) does not handle resources prudently. Utilizing a corporate fiduciary for the Lifetime Trust eliminates all such problematic issues.

In addition to the Lifetime Trust plan, there are a number of other viable techniques to mitigate a family's total death tax cost over multiple generations.

Article VII

Foreign citizens with Florida connections

Foreign citizens who seasonally or permanently reside in Florida, or own Florida real estate, are often under the impression that they are exempt from the federal estate and gift tax regime. However, this is often not the case – and a failure to adequately plan for the transfer tax can produce unexpected and expensive results. In fact, Trusts and Estates reports non-U.S. citizens routinely fail to sufficiently plan for the U.S. gift and estate tax system, noting the "extraordinarily high costs of not planning."

One question every foreign citizen must consider is whether he or she is a "resident" of the U.S. for gift and estate tax purposes. Under federal gift and estate tax law, a person is a U.S. tax resident if he has his "domicile" in the U.S. – even if he or she doesn't hold a green card. Under IRS rules, a person obtains a U.S. domicile by living here for any period, however brief, with no definite intention to move elsewhere. Surprisingly, the IRS position is that even non-immigrant visa holders may be treated as U.S. tax residents. Consequently, the determination of domicile is often a matter of dispute between the IRS and wealthy foreign citizens and their estates. And if a person is a resident for U.S. gift and estate tax purposes, then his or her *worldwide* estate is subject to this tax system.

For non-residents, the U.S. gift and estate tax system is applicable only to "U.S. property." Also, important loopholes in non-resident tax law offer forward-looking non-residents significant planning opportunities to minimize or eliminate tax liability.

Specifically, the federal gift tax applies to gifts a non-resident makes of U.S. property (subject to any applicable exclusions or deductions). For gift tax purposes, U.S. property generally includes tangible personal property (including cash) and real estate located in the United States. Intangible assets, including stock in a U.S. company, are not considered U.S. property for non-resident gift tax purposes. However, for estate tax purposes, a non-resident's "U.S. property" is more broadly defined and includes stock in a U.S. company and many other assets as well.

Surprisingly, a non-resident is not entitled to any gift tax exemption and only a $60,000 estate tax exemption. The lack of significant non-resident tax exemptions can produce disastrous tax results to a wealthy non-resident who owns or transfers U.S. property. Therefore, non-resident situations require careful advance planning – such as converting U.S. property to foreign property before death or becoming a U.S. resident to obtain the larger exemption ($5 million as adjusted for inflation).

Prospective foreign transplants to Florida should strongly consider utilizing an Asset Protection Trust prior to becoming a U.S. resident so that their estates are reduced prior to embracing the gift and estate tax regime. Importantly, Key Private Bank has extensive trust operations in states with highly favorable asset protection trust statutes, and these trust structures can be implemented with the assistance of Key Private Bank's trust team in Florida.

Also, any estate is entitled to an unlimited estate tax deduction for property passing to a surviving spouse if that spouse is a U.S. citizen. This critical deduction protects the "marital estate" from estate tax liability until both spouses are deceased. However, this deduction is not available if the surviving spouse is a foreign citizen unless the survivor's inheritance is placed in a highly restrictive qualifying trust. Consequently, if one or both spouses are foreign citizens, it is of great importance to take steps to protect the first-to-die spouse's estate from the estate tax.

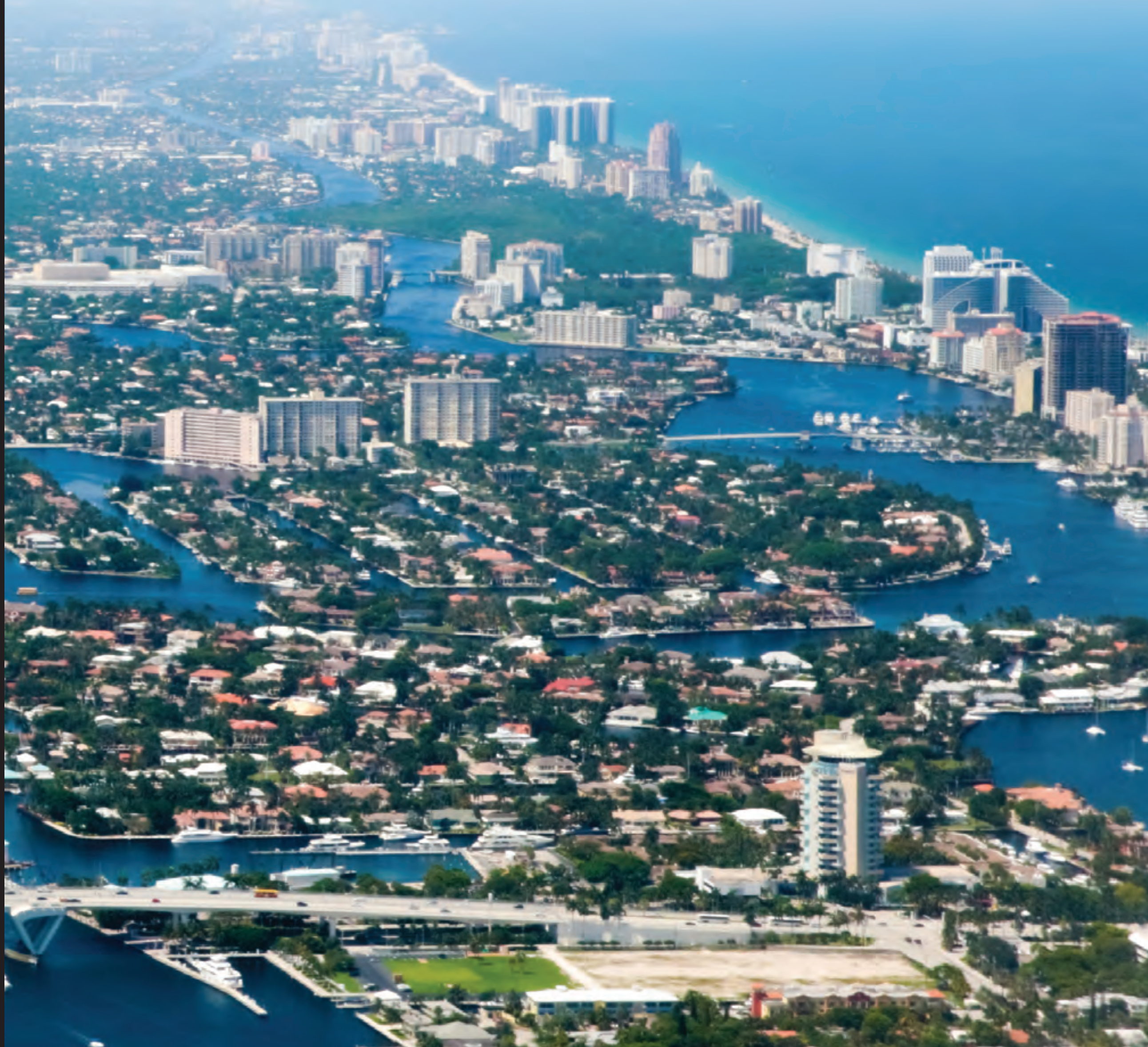
Further, tax treaties exist which may alter the general rules discussed above.

Finally, U.S. estate planning for the wealthy foreign citizen can be a complicated and extensive process. And, although a complete analysis of estate planning for the foreign citizen is beyond the scope of this material, it is nevertheless critical that the foreign citizen be highly pro-active and take sufficient legal steps, both with U.S. and foreign legal counsel, to ensure that an appropriate estate and tax plan is implemented.

ARTICLE VIII

Summary

Florida's popularity as a retirement destination will likely continue well into the 21st century and beyond. And regardless of whether you are a newcomer to Florida or a longtime resident of the Sunshine State, it is critically important that you have a Florida estate plan in order – both to properly establish a Florida tax residency and, even more, to ensure that your wishes at death and concerns for your heirs are properly addressed. Key Private Bank has a long-standing history of providing full-service investment management to its clients as well as serving as a professional Executor and Trustee for their estates and trusts. If the officers at Key Private Bank or the author of this guide may be of assistance to you, please do not hesitate to contact us.
It would be our pleasure to help you.



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