Jeff Baskies: Beware of Ad Valorem Tax Malpractice Trap when Transferring Clients' Florida Non-Homestead Real Property to LLCs & Trusts

"A very recent Florida 3rd DCA opinion, highlights a 'new' risk associated with transferring clients' Florida non-homestead residential real properties to LLCs or trusts – such transfers may trigger a significant increase in annual ad valorem property taxes. The increase in ad valorem taxes comes from the change of ownership causing the clients to lose their built-up non-homestead, 10% ad valorem residential property tax cap benefit (the benefit of their 'Assessment Limitation').

This new case highlights how very standard and maybe even 'typical' advice (e.g., 'You should transfer that Florida rental property you own into an LLC to protect your other assets in case of a slip and fall on the property.') might lead to an unintended but quite costly consequence – a doubling or more in ad valorem real property taxes in the year following the deed and then a much higher base for annual assessments annually following the loss of the Assessment Limitation.

Advisors should be aware of this issue (highlighted by this new case and the 3rd DCA's decision) to ensure they do not give advice that unwittingly costs their clients a huge increase in ad valorem taxes – to make sure they do not fall into this clear malpractice trap!

Jeff Baskies provides members with commentary that examines the "hot off the presses" case of *S and A Property Investment Services, LLC v Pedro Garcia et al (Miami-Dade County Property Appraiser) (FL 3rd DCA case No. 3D22-835, issued March 15, 2023).*

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Here is his commentary:

EXECUTIVE SUMMARY:

Many advisors - including out of state advisors with clients in Florida - know that Florida homestead property attracts myriad benefits (including potentially very significant ad valorem tax benefits – the 3% per annum Save Our Homes ('SOH') tax increase cap) and proceed cautiously before transferring homestead properties (to LLCs, trusts or otherwise).

Many advisors - including out of state advisors with clients in Florida - may also know that Florida has significant documentary stamp ("doc stamps") taxes (approximately $7,000 per $1 million of consideration), and that funding real property into trusts and/or LLCs may trigger doc stamps. However, generally, it is well known that there are certain exceptions allowing funding of trusts or LLCs without triggering doc stamps, for un-encumbered properties.

A very recent Florida 3rd DCA opinion (as noted it just came down March 15, 2023 and is not yet final), highlights a "new" risk associated with transferring clients' Florida real properties to LLCs or trusts – loss of the built-up non-homestead, 10% ad valorem residential property tax cap benefit (the Assessment Limitation). While this risk has been around since 2009, and so it isn't really 'new", it has garnered much less attention than the homestead SOH exemption, as it is a 10% cap that applies only to non-homestead properties (such as vacation homes, secondary residences, rental properties, commercial properties or vacant land). However, as Florida property values seem to be rising quite rapidly, tripping up the 10% Assessment Limitation is still properly considered a primarily "new" issue.

S and A Property Investment Services, LLC v Pedro Garcia et al highlights how "typical" advice (e.g., "You should transfer that Florida rental property you own into an LLC to protect your other assets in case of a slip and fall on the property.") might lead to unintended but quite costly consequences.

Advisors of Florida clients (or advisors of clients who own Florida real properties) should be aware of this decision to ensure they do not fall into this malpractice trap.

FACTS:

In 2000, Sylvester and Angela Anderson purchased a non-homestead property in Miami (the "Property"), as tenants by the entireties ("TBE"). In 2015, they established S and A Property Investment Services, LLC (the "LLC") - Angela owns 51% of the LLC while Sylvester owns 49%.

In June of 2019, in what might be considered a fairly standard asset protection plan, the Andersons deeded the Property to the LLC, to insulate themselves from any personal liability from owning the Property personally/directly. There was no consideration for the transfer to the LLC (which means the deed was just to fund the LLC and not to transfer interests in the LLC to anyone other than the Andersons and also the property was not encumbered at the time of the deed).

While a homestead property transfer could have triggered a loss of the 3% SOH cap benefits, this was not the Andersons' homestead property.

However, please be aware that the 3% annual cap for homestead property is not the ONLY Florida ad valorem tax cap for real property.

There is also a 10% per annum increase cap on non-homestead residential properties (the Assessment Limitation identified herein). And that was the issue in the case, because prior to funding the LLC, the Andersons enjoyed the benefit of the 10% Assessment Limitation cap for non-homestead residential property on the Property. But once they funded the LLC in 2019, the Property Appraiser for Miami Dade county re-assessed the Property at its then full, "just value" (the fair market value as determined by the Property Appraiser without regard for the built-up Assessment Limitation – thus ignoring the prior10% cap on increases in value.

Said differently, in the year after the deed to the LLC, the Property Appraiser removed the 10% property tax cap limitation the Andersons had enjoyed, and increased the taxes for the LLC. Per the decision, the Property Appraiser's assed value of the Property rose from $104,023 (with a 10% per annum cap on increases) to $273,409 in 2020, causing a 160%+ increase in property taxes for the same Property in 2020.

The LLC appealed this tax increase to the Value Adjustment Board ("VAB") challenging the removal of the 10% Assessment Limitation cap. The VAB ruled for the property appraiser.

The LLC then filed a complaint in circuit civil court adverse the Property Appraiser. Via cross-motions for summary judgment, the Andersons argued (by affidavit of Angela) that the funding of the LLC was a mere transfer "between legal and equitable title" and thus was not a "change of ownership" which is a pre-requisite to the right to re-assess the property under FS 193.1554(5). After an April 18, 2022 hearing on the competing motions for summary judgment, the court quickly issued a summary judgment in favor of the Property Appraiser (on April 26, 2022). The trial

court held that nothing in the deed or in the LLC's operating agreement indicated that the Andersons retained equitable title in the Property. That summary judgment was appealed.

As the 3rd DCA recited, FS 193.1554(3) provides that any change resulting from the annual assessment of a non-homestead residential property is capped at 10% of the assessed value of said property for the prior year – that's how the Assessment Limitation works. Further, the property will retain this 10% Assessment Limitation so long as the property does not undergo a "change of ownership or control" as per FS 193.1554(5), but if there is a change of ownership or control, then the property "shall be assessed at just value as of January 1 of the year following such change in ownership and control." FS 193.1554(5).

That statute contains 4 exemptions, and the one concerning in this case was this: "There is no change of ownership if …the transfer is between legal and equitable title". FS 193.1554(5)(b).

To support their argument that there was no change of ownership in this case, the Andersons cited to two doc stamp cases: Crescent Miami Center, LLC v. Fl Department of Revenue, 903 So. 2d 913 (Fla. 2005) and Kuro, Inc. v State Department of Revenue, 713 So. 2d 1021 (Fla 2d DCA 1998). Those cases support the position that a transfer of real property between a grantor and an LLC that is wholly owned by the grantor, absent any exchange of value and any mortgage, is considered without consideration and thus exempted from doc stamps under FS 201.02(1).

The Andersons asserted their transfer via deed to their LLC was essentially identical to the transfers in those Crescent Miami and Kuro, in which it was held in a transfer to an LLC wholly owned by the grantor the beneficial ownership remained unchanged.

The 3rd DCA noted that Crescent Miami and Kuro dealt with doc stamp liability under a different statute - F.S. 201.02, which taxes situations when there is a "purchaser" and "consideration" which is different from the inquiry under FS 193.1554(5)(b), which simply addresses a "change of ownership".

The court found the deed from the Andersons as TBE to the LLC (even though owned 100% by the Andersons) was a change of ownership. The LLC is a legal entity and it is separate and distinct from the individual owners prior to the deed to the LLC.

Finally, the Andersons urged the court to find that the deed was merely a change from "legal and equitable title" (falling into the exception in FS 193.1554(5)(b)). They asserted legal title went to the LLC, but they retained beneficial title.

You could give the Andersons an A for effort but ultimately their argument (at least thus far) failed.

The 3rd DCA stated that in its view the "Taxpayer's argument misapprehends the effect of a quitclaim deed, Florida LLC law, and equitable ownership."

With language like that, you know the holding wasn't going to go well for the Andersons, and it did not.

COMMENT:

Lessons can be gleaned from this decision.

First, while the 3% SOH/homestead ad valorem tax cap gets the bright lights and a lot of press, don't sleep on the 10% Assessment Limitation. Especially in periods of exponential property value increases (as we've been experiencing in Florida), even non-homestead properties may have significant built-up ad valorem tax Assessment Limitations. Planners must be aware of the cost to clients if those limits are lost – before clients fund LLCs or trusts or other entities with their non-homestead Florida residential real property.

Second, planners must also be careful of knee-jerk asset protection planning or probate avoidance planning. For clients who may live and own secondary or rental properties or for non-Florida-resident clients who own non-homestead properties (whether they be vacation properties, rental properties or some other type of property), reflexively advising some change of ownership can be catastrophic (tax-wise). Instead, planners must be aware of the 10% Assessment Limitations that may apply to such properties and account for them ***before*** deeding properties to trusts, LLCs or other structures.

For clients funding revocable trusts, their deeds to revocables trust should not be an issue. Thus, especially for non-Floridians transferring assets to revocable trusts to avoid probate, this holding should not alter good advice or planning.

But this case is a cautionary tale for advisors who hear "I have a rental property I own" and reflexively respond "Shouldn't we put that into an LLC?" Go slowly and fully understand the costs.

Third, transfers to irrevocable trusts, Limited Partnerships, LLCs or other business entities fall into this potential malpractice trap, so please be sure you do not.

Fourth, although not expressly part of the 3rd DCA opinion, the logic of S and A Property Investment Services, LLC v Pedro Garcia et al may also apply to situations where clients move to Florida and seek to apply for a homestead SOH exemption. FS 193.155 is the "save our homes" or SOH 3% homestead ad valorem tax cap statute. FS 193.155 states that "Property receiving the homestead exemption after January 1, 1994, *shall* be assessed at just value as of January 1 of the year in which the property receives the exemption …." (emphasis added) Thus, it would appear that any pent-up benefit of the 10% Assessment Limitation is forfeited for a client who perhaps owned a Florida vacation property that she or he decides to move into as a primary residence, if such client applies for a homestead exemption.

Again, this is a potential trap for the unwary and should be considered and understood. In the long run, the benefit of the 3% per annum cap may well exceed any lost benefit from forfeiting the 10% Assessment Limitation, but it is best to consider such and discuss it with your client before the client seeks a homestead exemption.

Finally, although it was not expressly addressed in the Opinion, it is fair to wonder if the 3rd DCA may have reached an alternate result if the ownership of the LLC by the Andersons was identical to their ownership of the Property – before it was deeded to the LLC. Again, the facts in S and A Property Investment Services, LLC v Pedro Garcia et al were: the Andersons owned the Property 100% as tenants by the entireties but they owned the LLC 51% by Angela and 49% by Sylvester. The lack of identity of ownership may have undercut the Andersons argument to apply the exception in FS 193.1554(5)(b) – the Andersons argument that funding the LLC was a mere transfer between legal and equitable title.

If clients create an LLC and own it in the exact same proportions as they own the property they deed into the LLC, perhaps they can argue for the application of the exception in FS 193.1554(5)(b), arguing there was a mere transfer between legal and equitable title.

However, in its Opinion, the 3rd DCA did not say there was an exception for transfers to LLCs, and the 3rd DCA did state that LLCs are separate entities from their owners. Remember the 3rd DCA stated: "Taxpayer's argument misapprehends the effect of a quitclaim deed, Florida LLC law, and equitable ownership." So that language could still be concerning, even while one may wonder if identical ownership would have led to a different result.

To be safe, however, until it is made clear that having identical ownership will in fact avoid a revaluation and not cause a loss of the Assessment Limitation, it seems prudent to be careful before tempting fate with such a deed to an entity. Yet, if one were contemplating funding a property into an LLC that had a built-up Assessment Limitation benefit, certainly a phone call to the Property Appraiser's office would be in order.

It would be interesting to know if a transfer to an LLC with identical ownership is exempt from the revaluation.

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Jeff Baskies

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S and A Property Investment Services, LLC v Pedro Garcia et al (Miami-Dade County Property Appraiser) (FL 3rd DCA case No. 3D22-835, issued March 15, 2023). (The decision is not yet final and the author does not know if there will be a request for rehearing or appeal); : Crescent Miami Center, LLC v. Fl Department of Revenue, 903 So. 2d 913 (Fla. 2005); and Kuro, Inc. v State Department of Revenue, 713 So. 2d 1021 (Fla 2d DCA 1998).