by Ronald H. Kauffman

Underwater Treasure: Equitable Distribution of the "Save Our Homes" Limitation

Did anyone notice there is a new marital asset? This new asset is easy to overlook because nearly half of Florida homes are sunk in negative equity.[1] When the real estate market recovers, family lawyers may discover there is a brand new asset to distribute: the homestead tax assessment limitation, which is now portable.

One of the largest exemptions Florida homeowners are entitled to is the homestead exemption, which can now shield up to $75,000 of the value of a home before its taxable value is determined.[2] The homestead exemption is found in Fla. Const. art. VII and provides a tax exemption up to the assessed valuation of $25,000 and, for all levies other than school district levies, on the assessed valuation greater than $50,000 and up to $75,000, in certain circumstances.[3]

The "Save Our Homes" Amendment (SOHA) is found in Fla. Const. art. VII, §4(d)(1), and SOHA essentially caps any increases in your home's assessment to the lower of three percent of the assessment for the prior year, or the percent change in the Consumer Price Index. Last year, SOHA protected roughly $180 billion in assessed value from taxation.[4]

Prior to 2008, the SOHA assessment limitation ended when ownership of the homestead changed.[5] In 2008, voters approved Amendment 1 to the constitution, which allows homeowners to keep a portion of their SOHA differential after their home is sold, and transfer that portion to a new homestead. Fla. Const. art. VII, §4(d)(8) provides, in pertinent part:

> a. A person who establishes a new homestead as of January 1, 2009, or January 1 of any subsequent year and who has received a homestead exemption pursuant to Section 6 of this Article as of January 1 of either of the two years immediately preceding the establishment of the new homestead is entitled to have the new homestead assessed at less than just value. If this revision is approved in January 2008, a person who establishes a new homestead as of January 1, 2008, is entitled to have the new homestead assessed at less than just value only if that person received a homestead exemption on January 1, 2007.

The constitutional provision, which is implemented in F.S. §193.155, is most noticeable when the real estate market crests, as it keeps property taxes down while market values go up. The inverse is true when real estate prices hit bottom. Today, we are experiencing SOHA's recapture rule, in which taxable values rise while market values sink. Since Amendment 1 passed, its family law implications have lain hidden under a sea of stagnated property values and weak sales.[6]

SOHA Portability: Tax Consequence or Marital Asset?

The new ability to transfer the SOHA differential creates a classification problem in family law: Is it a tax consequence of the sale of the home, or is it a marital asset which is now distributable? The distinction between a tax consequence and asset is important because a court only has to consider the tax consequences of a distribution, but must actually distribute the marital assets.

On the one hand, SOHA portability could be construed as a tax consequence imbedded in, and unlocked by, the sale of the marital home. In the event of a sale of the marital home, both spouses take their SOHA differential to new homes, and classifying the benefit as a tax consequence makes sense.

In Florida, the tax consequences in every distribution must be taken into consideration to achieve a fair and equitable result.[7] The reasoning is simple: Consideration of the tax impact of an equitable distribution plan prevents a party from gaining an unfair advantage or suffering an unfair burden.[8] Additionally, valuing a property without considering its tax consequences does not accurately reflect its fair market value.[9]

In *Sweeney v. Sweeney*, 583 So. 2d 398 (Fla. 1st DCA 1991), the First District directed a trial court on remand "to consider whether there will be tax consequences for either party as a result of filing an individual return, which *should* be taken into consideration when reevaluating the entire equitable distribution."[10] In *Nicewonder v. Nicewonder*, 602 So. 2d 1354 (Fla. 1st DCA 1992), the court elaborated that a trial court is required to consider the consequences that affect the value of the properties being distributed, including contingent tax liabilities.[11]

However, in *Doyle v. Doyle*, 789 So. 2d 499 (Fla. 5th DCA 2001), the court concluded that no reversible error had occurred in failing to consider income tax consequences, because the wife failed to present evidence on the issue at trial.[12] For underreported and obscure tax issues, such as SOHA portability, *Doyle* serves as a warning to present evidence of all tax consequences of a distribution at a trial, or

run the risk that a court's failure to consider them may not be correctible on appeal.[13]

In addition to the risks of characterizing SOHA as a tax consequence, sometimes there is no sale, or only one party ends up with the home. In those cases, classifying SOHA as a tax consequence of a sale is futile because there is no sale, and it also overlooks the value of SOHA portability. Because of these risks and problems, it may make more sense to classify SOHA's tax savings as a marital asset to be distributed.[14]

Calculating SOHA Portability When Splitting

The SOHA benefit varies by the differences in the values of the old and new homesteads as of January 1 in the year the old homestead was abandoned.[15] The amount of any assessment limit you can transfer will depend on whether you are "upsizing" or "downsizing," or whether there is even a differential to port.[16] In all cases, the maximum benefit which can be transferred to a new homestead is $500,000.[17]

In the two calculations below, the parties are "splitting" — meaning the people who shared a homestead abandon it and establish separate ones.[18] Assume the parties have met the requirements for receiving their homestead and that the former home had a just value of $400,000, an assessed value of $300,000, with an assessment difference of $100,000.

In the upsizing case, the law provides a dollar-for-dollar portability. If each party buys a new homestead with a just value of $500,000, each party will be able to port their $50,000 half of the full assessment difference of $100,000 to their new homesteads. The parties' new homesteads would each have an assessed value of $450,000.

The downsizing rule is different because the statute only allows for proportional portability. The transfer amount is calculated to be the same proportion of the assessment difference in the previous homestead of the just value of the previous homestead. Assuming the parties' new homesteads each have a just value of $250,000, the SOHA difference to port would be (50,000/400,000) x 250,000 = 31,250. Each new homestead would then have an assessed value of $218,750 (250,000 – 31,250 = 218,750).[19]

Who Benefits from SOHA Portability After Splitting and Who Does Not?

The Department of Revenue is the administrative agency charged with enforcing, interpreting, and establishing procedural rules related to taxes. The department has only promulgated Rule 12D-8.0065 in draft form.[20] Instead, the department has been operating under its emergency rules since passage of Amendment 1.[21] As you will see, the department's rules do not merely shed light on the Constitution; the rules refract the language. There are a few examples that should concern family lawyers.

• *Jointly Titled Marital Property: Both Spouses Abandon the Homestead* — The first example involves a husband and wife who own a home titled in both names. After divorcing, the parties sell the home and move out. The parties have two assessment years from the sale to establish new homesteads and transfer their SOHA differentials to their new homes. In this scenario, the couple would each port their half of the SOHA differential to their new homestead properties as shown in the calculations above.

What if the parties want to agree to an unequal distribution of SOHA? The justification for dividing the SOHA benefit unequally is not much different from awarding the child dependency exemption to one spouse. Arguably, the person awarded the SOHA cap may have more disposable income through lower property tax payments and a greater ability to pay support. Alternatively, the SOHA savings would allow the awarded spouse a greater ability to meet living expenses and perhaps have less need for support.

However, the Department of Revenue, under Emergency Rule 12DER08-33(5)(b), has interpreted the statute to mean: "the shares of the assessment limitation difference *cannot be sold, transferred, or pledged to any person*. For example, a husband and wife

divorcing and both abandoning the homestead would each take their share of the assessment limitation difference and the property appraiser could not accept a stipulation otherwise." (Emphasis added.)

In light of the department's interpretation, an amendment to the statutory language would be required to accommodate splitting the SOHA benefit unequally in a marital settlement agreement or to allow a court to equitably distribute the SOHA benefit.

• *Jointly Titled Marital Property: One Spouse Remains in the Homestead* — The second example is more interesting because in this scenario, one party stays in the marital home. In many cases, someone is awarded the marital home in an equitable distribution, or for exclusive use and possession pursuant to F.S. §61.075(1)(h). The procedures to port the SOHA differential become murkier when one party remains in the homestead.

Classifying the SOHA cap as a tax consequence of a sale if a party is remaining in the home renders SOHA portability irrelevant because the property is not sold. Portability is only triggered by the abandonment and reassessment of the old homestead and the establishment of a new homestead.[22] If one party remains in the marital home, the prior homestead has not been abandoned and the remaining spouse keeps the house, the tax limit, and the ability to port it. The other spouse takes nothing.

One possible way to distribute the SOHA benefit involves both parties abandoning the prior homestead with one party keeping the home as a primary residence.[23] The typical way of changing ownership in divorces — exchanging quitclaim deeds between spouses — may not be enough to abandon the homestead. The statute specifically excludes transfers between husband and wife as a change of ownership.[24] In order to abandon the homestead, the spouse remaining in the home would have to notify the property appraiser of their abandonment and have it re-assessed, then apply to port the assessment difference back onto the prior homestead.[25] A review of the legislative history indicates that one of the purposes of the 2008 amendment to §193.155 was to accomplish exactly this result.[26]

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Abandonment is risky, as it would cause the marital home to be reassessed for tax purposes. Moreover, abandonment and reassessment do not take place in the middle of the calendar year.[27] In the event the court has already entered a final judgment of dissolution of marriage, the remaining spouse may likely be the sole owner, and there may not be another spouse to which to transfer a differential.

A proposed solution is to classify the SOHA benefit as a marital asset rather than a tax consequence. The SOHA benefit could itself be distributed, without having to abandon or sell the homestead. Under this alternative, SOHA is analogous to capital loss carryovers.[28] Generally, a capital loss carryover is the ability to carry over a capital loss incurred in one tax year, and deduct the loss in future tax years under certain conditions. Today, there is already one reported Florida decision where capital loss carryovers have been recognized as marital assets.[29] For SOHA purposes, one spouse vacates the homestead, and that spouse would be entitled to a credit or setoff in the equitable distribution plan — or lump sum alimony — to compensate for his or her inability keep the SOHA benefit. The other spouse would keep the homestead and the SOHA differential entirely.

• *Jointly Titled Property*: *Cohabitation* — The third example involves unmarried homesteaders, who have the most perilous position. The ability to transfer an assessment limitation when joint title holders are not married is determined by who actually applied for the homestead exemption, not necessarily who is on title or who remains in the prior homestead.[30]

Increasingly, cohabitating partners buy homes and title them in both names without marrying.[31] One of the parties may have a problem porting their SOHA differential. F.S. §193.155(8) (emphasis added) states: "Property assessed under this section shall be assessed at less than just value when *the person who establishes a new homestead* has received a homestead exemption as of January 1 of either of the 2 immediately preceding years."

The department interprets the "person who establishes a new homestead" as the person who applied for homestead exemption so that only the applicant for the homestead exemption is entitled to the SOHA benefit.[32] The department's "applicant only" rule impacts any cohabitatant, and perhaps former spouses, seeking portability. Married homesteaders do not face this problem. In June 2008, F.S. §193.155(8) was specifically amended to provide that both the husband and wife are each deemed to have received the homestead exemption, even though only one of them applied.[33]

Conclusion

It is not every day that one witnesses the birth of a totally new marital asset. Amendment 1 became effective in 2008 as Florida's real estate market was sinking. That same year, over 42,000 Floridians successfully transferred approximately $3 billion in homestead differentials.[34] The constitutional provision requires further amendment to more equally treat modern families, and to allow for a more equitable distribution of SOHA's benefits. Learning to navigate Amendment 1 will help our clients salvage their underwater treasure.❑

[1] *See* CoreLogic, *Second Quarter Negative Equity Report*, August 25, 2010, http://www.corelogic.com/uploadedFiles/Pages/About_Us/ResearchTrends/CL_Q2_2010_Negative_Equity_FINAL.pdf.

[2] *See* FLA. STAT. §196.031(7) (2009). Other exemptions, such as the veterans, disability, religious, educational, and charitable exemptions, could exempt the value of the whole property.

[3] *See* FLA. CONST. art. VII, §6(a).

[4] *See* Florida Department of Revenue, Publications and Data, *2009 Florida Property Valuations and Tax Data Book*, Table 41, http://dor.myflorida.com/dor/property/rp/databk.html.

[5] *See* FLA. CONST. art. VII, §4(d)(3). *See also* FLA. STAT. §193.155(3)(a) (2009).

[6] The S&P/Case-Shiller Composite actually showed U.S. home prices posting a modest gain in its June 2010 index. However, price levels remain close to April 2009 lows. *See* S&P/Case-Shiller Composite 20 Home Price Index, *available at* http://www.standardandpoors.com/indices/sp-case-shiller-home-price-indices/en/us.

[7] *See Nicewonder v. Nicewonder*, 602 So. 2d 1354, 1358 (Fla. 1st D.C.A. 1992).

[8] *See Vaccaro v. Vaccaro,* 677 So. 2d 918 (Fla. 5th D.C.A. 1996).

[9] *See Nicewonder*, 602 So. 2d at 1358.

[10] *See Sweeney,* 583 So. 2d at 399 (emphasis added).

[11] *See Nicewonder*, 602 So. 2d at 1357.

[12] *See Doyle,* 789 So. 2d at 504.

[13] *See id*.

[14] *See* FLA. STAT. §61.075(6)(a) (2009).

[15] *See* FLA. STAT. §193.155(8) (2009).

[16] *See* FLA. STAT. §§193.155(8)(a) - (b) (2009). Upsizing refers to buying a new homestead of greater or equal value to the immediate prior homestead. In downsizing, the new homestead is less than the just value of the immediate prior homestead. In an age where taxable values may be greater than or equal to the just value, there is no limit to port.

[17] *Id.*

[18] *See* F.A.C. Rule 12DER08-33(5)(b) (Jan. 7, 2009), *available at* Florida Department of Revenue, Publications and Data, Laws and Legislation, http://dor.myflorida.com/dor/property/legislation/erules.

[19] These calculations determine the SOHA differential transferable to a new homestead, not the value of the marital asset itself. For this and other examples *see* Department of Revenue, Calculation of Assessment Limitation Difference Transfer Amount, http://dor.myflorida.com/dor/property/legislation/amendment1/pdf/portfaqexamples.pdf.

[20] *See* F.A.C. Rule 12D-8.0065 (2009) (Draft Dec. 24, 2009), Florida Department of Revenue, Publications and Data, Laws and Legislation, http://dor.myflorida.com/dor/property/legislation/erules/pdf/12d80065draft.pdf (last visited October 1, 2010).

[21] *See* F.A.C. Rule 12DER08-33.

[22] *See* FLA. STAT. §193.155(8) (2009).

[23] *See* F.A.C. Rule 12DER08-33(6).

[24] *See* FLA. STAT. §193.155(3)(a)(2) (2009).

[25] *See* F.A.C. Rule 12DER08-33(5)(b).

[26] *See Senate Bill Analysis and Fiscal Impact Statement on CS/SB 1588* (April 2, 2008), stating: "A similar situation is that a couple gets a divorce and the husband moves to a new homestead. They want to split the assessment difference on their former home (the wife's current home), but the law requires that the previous homestead be abandoned before a transfer can occur. This could be accomplished if the wife could abandon her homestead as of the January 1st following their divorce and then the husband and wife each transfer their proportionate share (half) of the difference to their respective homesteads."

[27] *See* F.A.C. Rule 12DER08-33(2)(a)(2).

[28] *See* I.R.C. §1211 (2009).

[29] *See Haley v. Haley*, 936 So. 2d 1136 (Fla. 5th D.C.A. 2006). In *Haley*, the court found some of the capital loss carryovers to be marital, but reversed the trial court's distribution because a substantial portion of the losses resulted from a nonmarital, family partnership to which one spouse made no special contribution. The district court remanded to determine both distribution and valuation.

[30] *See* F.A.C. Rule 12DER08-33(2)(b)(2)-(3).

[31] Nationwide, married-couple households decreased to 51 percent from 71 percent of all households from 1970 to 2007. During the same period, other family households and nonfamily households increased to 49 percent from 29 percent of all households. See U.S. Census Bureau, *America's Families and Living Arrangements: 2007* (Sept. 2009), http://www.census.gov/population/www/socdemo/hh-fam/p20-561.pdf.

[32] A comparison between the Emergency Rules promulgated by the Department makes the difference between married and unmarried joint title holders perfectly clear. *Compare* F.A.C. Rule 12DER08-33(2)(b)(1): "For a husband and wife who owned, shared and both resided on, a previous homestead, *each shall be considered to have received the homestead exemption . . ." with* F.A.C. Rule 12DER08-33(2)(b)(2): "For joint tenants with right of survivorship, those tenants *that applied for* . . . the homestead exemption . . . shall be considered to have received the homestead exemption…[italics added]."

[33] *See* FLA. STAT. §193.155(8).

[34] *See* Florida Department of Revenue, Publications and Data, *2008 Homestead Property Portability Impact Data,* http://dor.myflorida.com/dor/property/legislation/amendment1.

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