

Re: Florida Community Property Trust

July 1, 2025

A. What is an FCPT and how does it work?

1. Pursuant to Florida statute enacted in 2021, a Florida Community Property Trust (FCPT) is a trust created by and signed by both spouses as settlors (with the execution formalities required for the execution of a trust in Florida) containing assets transferred by them to the trust. The trust must declare that it is a Community Property Trust. The Trust must be managed by at least one “qualified trustee,” which is a Florida resident individual trustee or a company authorized to function as trustee in Florida. The spouses may serve as co-trustees with the qualified trustee if they are not Florida residents. There is no express requirement contained in the statute that the settlors be Florida residents in order to set up the FCPT. Finally, the trust agreement must contain language (in capital letters) at the beginning of the trust regarding consequences for the spouses upon entering into the FCPT.

2. The primary purpose of an FCPT is to achieve full step-up in basis of the entire trust property at the death of the first spouse/settlor to die (see below).

3. The FCPT may include provisions for the management of the trust, the revocability of the trust, and planning for contingencies of death, divorce, or the occurrence of an event, subject to:

a. Upon death of a settlor, one-half of the aggregate value of the assets contained in the trust is subject to testamentary disposition by the decedent and one-half of the aggregate value of the assets in the trust is not subject to such disposition.

b. Upon divorce, the trust is terminated and each spouse will receive one-half of the trust assets.

c. Unless otherwise provided in the trust agreement, the trust may be revoked by either spouse during their joint lifetimes. During the joint lifetimes of the settlors, the trust may be made to be irrevocable pursuant to the statute. However, making the trust irrevocable is not recommended due to potential tax consequences. Furthermore, even if the agreement states that the trust is irrevocable, the statute requires that, after the death of the first spouse/settlor, the surviving spouse/settlor may nonetheless revoke one-half of the trust.

d. During the joint spousal lifetimes, only the spouses can be beneficiaries of the trust. After the death of the first spouse/settlor, the surviving spouse can be the only beneficiary of that spouse’s one-half share.

e. Although the statute permits the trustee to make non pro rata distributions of property (as opposed to distributing equal shares of property to the spouses), better practice typically is for the trust to require pro rata distributions to avoid potential tax issues.

f. The statute provides that an FCPT is unenforceable if it was a result of fraud, duress, coercion or overreaching, is involuntarily executed, is unconscionable, or the spouse against which the trust is to be enforced did not receive disclosure of the property forming the trust, did not waive that disclosure, or did not have notice of the property of the other spouse.

g. Separate legal representation is not required by statute. However, separate counsel for the two spouses in some circumstances is preferable.

h. The FCPT as a joint revocable trust may be simply structured, so that upon the death of the first spouse/settlor, his or her one-half share could pass to another separate inter vivos (revocable) trust containing his or her estate planning provisions (after achieving full step-up in basis). The survivor could then, after enjoying full step-up in basis for his or her one-half share, transfer his or her share to a different inter vivos (revocable) trust containing his or her estate planning provisions.

B. Tax advantage of the FCPT

1. If a married couple owns assets jointly, Internal Revenue Code (IRC) section 2040 includes one-half of the fair market value of the joint assets in the estate of the first to die. As to the joint assets included under IRC section 2040, IRC section 1014(a)(1) gives a step-up in basis to the decedent for one-half of the fair market value of the assets owned jointly.

2. If assets are held in an FCPT, IRC section 1014(b)(6) should provide a step-up in basis to the surviving spouse's one-half share of the property. Combining this one-half step up as to the surviving spouse's share with IRC section 1014(a)(1)'s step-up in basis as to the decedent's one-half share of the property means that all of the property in the FCPT should receive a full "double" step-up in basis upon the death of the first to die.

Issues with the use of IRC section 1014(b)(6)

IRC section 1014(b)(6) has not been used directly by the IRS to bless the FCPT. This Code section states simply that it applies to "property which represents the surviving spouse's one-half share of community property held by the decedent and the surviving spouse under the community property laws of any state, or possession of the United States or any foreign country, if at least one-half of the whole of the community interest in such property was includible in determining the value of the decedent's gross estate under Chapter 11 of subtitle B (section 2001 and following, relating to estate tax) or section 811 of the Internal Revenue Code of 1939."

1. One commentator takes the position, while analyzing IRC section 1014(b)(6), that "...if a state incorporates characteristics of the community property statutes from the eight original community property jurisdictions, it should be respected by the Tax Court or the IRS."

2. An IRS field advisory from 1993 provides that community property brought to a common law state retains community property treatment and a surviving spouse would have a step-up basis in the entire property, rather than just one-half.

3. In a 2020 guidance provision, however, an IRS publication states that "...Tennessee and South Dakota passed elective community property laws. This publication does not address the federal tax treatment of income or property subject to the community property election."

4. Considering that there is no express blessing by the IRS or case law for the FCPT, the more conservative practice would be to limit its use to residents of Florida, using assets other than non-Florida real property. Potential homestead restrictions should be considered if Florida real property is used.

5. An FCPT may be able to be used for non-residents of Florida, given that the Florida statute does not expressly limit its application to Florida residents. All of Tennessee, Alaska and South Dakota do expressly allow nonresidents to use their respective Community Property Trust statutes. However, use in the case of a non-resident of Florida increases the risk that the IRS may deny full step-up in basis.

6. Finally, if spouses were to create an FCPT and the IRS takes the position that full step-up in basis is not available, they should be no worse off than had they not created the FCPT. The surviving spouse may challenge the IRS in court through federal tax litigation.

D. Other factors.

Other factors to consider before the creation of an FCPT are:

- Extent to which the clients' assets are low basis.
- Likelihood of sale after death of first spouse/settlor.
- Potential advantages for alternative use of assets in inter vivos estate/gift tax strategies.
- Creditor issues.
- Stability of marriage.
- Common/shared client estate planning goals.

For the right situation, an FCPT may be a potent device to save significant capital gains tax.

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