The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Finance and Tax Committee

BILL: CS/CS/SB 2040

INTRODUCER: Finance and Tax Committee, Judiciary Committee, and Senator Geller

SUBJECT: Documents Excise Tax

DATE: April 21, 2008 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Maclure	Maclure	JU	**Fav/CS**
2.	ODonnell	Johansen	FT	**Fav/CS**
3.			GA	
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

A. COMMITTEE SUBSTITUTE..... [x] Statement of Substantial Changes
B. AMENDMENTS........................ [ ] Technical amendments were recommended
[ ] Amendments were recommended
[ ] Significant amendments were recommended

I. Summary:

This bill authorizes a person transferring unencumbered real property to their own legal entity to, by election, pay documentary tax either on the property's market value at the time of the transfer, or subsequently when there is either a change in the ownership interest in the property, or in any interest in the entity. If a subsequent transfer of the interest in the entity simply returns the property back to the original owner, with no change to their original ownership interest, no tax is due on that subsequent transfer. The document evidencing the election must be recorded at the time of the transfer.

This bill substantially amends section 201.02, Florida Statutes.

II. Present Situation:

Documentary Stamp Tax – Overview

The documentary stamp tax imposes an excise tax on deeds or other documents that convey an interest in Florida real property.[1] The tax rate is 70 cents on each $100 of consideration for deeds, instruments, or writings whereby lands, tenements, or other real property, or any interest therein, are granted, assigned, transferred, conveyed, or vested in a purchaser.[2]

Subsections (6) through (9) of s. 201.02, F.S., provide exemptions and limitations to imposition of the documentary stamp tax. These include:

- Transfers of real property from a nonprofit organization to specified governmental entities;
- Transfers of a marital home between spouses or former spouses as part of an action for dissolution of marriage; and
- Contracts to sell the residence of an employee relocating at his or her employer's direction, when the sales contract is between the employer and the employee.[3]

There is also a limitation applied to certain judicial sales of real property under a foreclosure order. The certificate of title issued by the clerk is subject to the tax; however, the amount of the tax is computed based on the amount of the highest and best bid received at the foreclosure sale.[4]

Conveyances from Grantor to Wholly Owned Grantee

Following 1990 legislation[5], DOR amended the Florida Administrative Code[6] to provide that a conveyance from a shareholder to a corporation in exchange for stock is subject to the documentary stamp tax. This revision reflected the Department's understanding of 1990 legislation. DOR's position was supported by a 2003 opinion of the Florida's 3rd District Court of Appeal.[7]

In 2005, the Florida Supreme Court addressed the question of whether the conveyance of property from a grantor to its wholly owned grantee was subject to the documentary stamp tax in *Crescent Miami Center, LLC v. Florida Department of Revenue*.[8] Under the facts of that case, Crescent Real Estate Equities formed Crescent Miami Center, LLC, and then transferred 99.9 percent of its interest in Crescent Miami Center to a subsidiary limited partnership that Crescent Real Estate Equities owned. The remaining 0.1 percent interest was transferred to another limited

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[1] Section 201.02(1), F.S.
[2] *Id*. A similar tax is also levied in s. 201.08, F.S., on a different tax base: certificates of indebtedness; promissory notes; wage assignments; and retail charge account agreements. See, Florida Senate, Florida House of Representatives, Office of Economic and Demographic Research, and Department of Revenue, *Florida Tax Handbook: Including Fiscal Impact of Potential Changes*, 53 (2008).
[3] Section 201.02(6)-(8), F.S.
[4] Section 201.02(9), F.S.
[5] Chapter 90-132, s. 7, L.O.F. (1990).
[6] Fla. Admin. Code Rule 12B-4.013(7).
[7] *Crescent Miami Center, LLC v. Florida Department of Revenue*, 857 So.2d 904 (Fla. 2003).
[8] *Crescent Miami Center, LLC v. Fla. Dep't of Revenue*, 903 So. 2d 913, 916 (Fla. 2005).

liability company. On the same day, the latter limited liability company transferred the 0.1 percent interest to the limited partnership so that the limited partnership became the sole owner of Crescent Miami Center. According to the Supreme Court:

> On February 25, 2000, Crescent Equities transferred a tract of real property … in fee simple to [Crescent Miami Center]. According to the deed, [Crescent Miami Center] paid ten dollars and "other good and valuable consideration" for the property. … The deed was recorded, and [Crescent Miami Center] paid $1,212,750 in documentary stamp tax, which was comprised of the state documentary stamp tax and a Dade County documentary surtax.
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> After paying this tax, [Crescent Miami Center] filed for a refund of the documentary stamp tax, but the Florida Department of Revenue (DOR) denied the application. [Crescent Miami Center] filed suit and asserted that it should not have been required to pay the tax because it was not a purchaser of real property under section 201.02(1). Since beneficial ownership of the property did not actually change, [Crescent Miami Center] argued, the transfer was a mere book transaction and thus not subject to the documentary stamp tax in section 201.02(1).[9]

The Supreme Court held that the documentary stamp tax did not apply to the transfer of real estate to a taxpayer owned solely by the grantor. The Court found "that the transfer of property between a grantor and its wholly owned grantee, absent any exchange of value, is without consideration or a purchaser and thus not subject to the documentary stamp tax."[10]

Some property appraisers and others have expressed concerns about the potential fiscal impact to the state because the types of transactions described in the *Crescent Miami Center* case are not subject to the documentary stamp tax.[11]

In fiscal year 2005-06, Florida's documentary stamp tax collections totaled roughly $4 billion - the second highest source after sales tax. Estimates for state fiscal year 2007-2008 and 2008-2009 are below $2 billion, largely reflecting continued weakness in the real estate market. In addition, however, it appears that a significant number of real estate transactions are being structured to allow real property sales to be recorded without incurring a documentary stamp tax liability. These transactions are structured to conform to what the Supreme Court found was not a taxable transfer in *Crescent Miami.*

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[9] *Id*. at 914-15.
[10] *Id*. at 919.
[11] *See, e.g.,* Jeff Ostrowski, *Critics push to plug drain in tax loophole*, Palm Beach Post, August 12, 2007, *available at* http://www.palmbeachpost.com/business/content/business/epaper/2007/08/12/m1a_TAX_LOOPHOLE_0812.html (last visited April 6, 2008).

Consequences of *Crescent*

The Supreme Court's opinion eliminates[12] documentary stamp tax on the recordation of transfers of real estate when unencumbered property is transferred to a corporation, or an LLC, that is owned by the same individual, or individuals, who own the property in the same ownership proportions. Examples include transfers from:

1. A corporation to a wholly owned subsidiary, or from a subsidiary to its sole corporate parent;

2. To an owner of single member limited liability company, or from a single member limited liability company to its sole owner;

3. From partners to a limited liability company in which the partners each own equal membership interests, or from a limited liability company to the partners.

As pointed out in the October 2005 issue of ***The Florida Bar Journal***[13], "in certain instances, practitioners could conceivably utilize *Crescent* to avoid the application of the documentary stamp tax on future transfers of real estate. A simple example demonstrates the planning potential in this area." The Journal article then provides the following example:

> Assume seller (*S*) and purchaser (*P*) have entered into a purchase and sale contract with a purchase price of $5 million in connection with the sale of real estate. Absent any documentary stamp tax planning, the sale of the real estate would generate documentary stamp tax of $35,000. However, the transaction could alternatively be structured as follows: 1) *S* contributes the real estate to a wholly owned special purpose limited liability company formed solely for the transaction (*S* LLC); 2) *S* then sells the membership interest in *S* LLC to *P* for the $5 million purchase price; 3) *P* then dissolves *S* LLC and takes title to the real estate. *S* and *P* end up in the same exact place, except that the documentary stamp tax has been avoided.

The author's opinion is that there is no documentary tax due under *Crescent* given the facts in the example when documents are recorded in the official records. In 2007, the Florida Department of Revenue published an Technical Assistance Advisement[14] in response to a question about the impact of *Crescent.* The Department's advisement appears to agree with the author's opinion that no tax is due on the recorded transfer of real property where the same owner of the property owns the real property in equal proportion after the transfer and there is no mortgage or other consideration given for the land.

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[12] Minimum tax is due.

[13] *Crescent—Did the Florida Supreme Court Effectively Repeal the Documentary Stamp Tax on Transfers of Real Estate?*, **Florida Bar Journal** (October 2005).

[14] TAA No. 07B4-004.

III. Effect of Proposed Changes:

This bill authorizes a person transferring unencumbered real property to their own artificial legal entity to elect to pay documentary tax on the property's market value at the time of recording the transfer, or at the time of any subsequent change in the ownership interest in the property, or at the time of any subsequent transfer of interest in the entity. If the subsequent transfer returns the property back to the original owner with no change, no tax is due on the subsequent transfer. The document on which the original election is made must be recorded at the time of the transfer.

The bill permits recordation of a transfer of real property from a grantor to a wholly owned grantee without the payment of documentary stamp tax under certain circumstance.[15] The bill amends s. 201.02, F.S., to prescribe the characteristics of a transaction to which an election applies. Such a transaction must meet three conditions:

- A deed transfers an interest in real property from the owner of an artificial legal entity to that entity;
- There is a mere change in the form of ownership without effecting any change in beneficial ownership interests; and
- The sole consideration for the transaction is an increase in the value of any ownership interests in the grantee entity.

If a transaction meets these conditions, the bill provides that the parties may elect to pay the documentary stamp tax otherwise due on the fair market price of the property at the time of the transfer or, in the alternative, tax may be paid on the fair market value of the property upon any subsequent transfer of an ownership interest in the grantee artificial legal entity, or an interest in the real property.

An exception to the requirement for payment on the subsequent transfer is provided when it represents a return of the interest in the real property from the artificial legal entity to the original owner, resulting in no change in the beneficial ownership interests previously held in the property.

When tax liability is triggered, the amount of consideration for purposes of calculating the tax due will be the greater of:

- Any increase in the value of any ownership interest in the grantee entity; or
- The fair market value of the interest in the real property at the time of the transfer.

Currently, the documentary stamp tax rate is 70 cents on each $100 of the consideration paid for a property transfer. The bill revises the definition of consideration under s. 201.02, F.S., to include any increase in the value of any ownership interest in a grantee entity, or any other entity. The bill provides that if consideration is not determinable at the time of the transfer, consideration is presumed to equal fair market value.
The bill specifies that tax collections resulting from the new provisions shall be deposited into the “Sadowski Affordable Housing Trust Fund.” There is no trust fund with this name currently

[15] *Crescent Miami Center*, 903 So. 2d at 919.

codified in the Florida Statutes. Also, there are existing statutory caps on the amount of money authorized for deposit into trust funds into which documentary stamp tax is currently distributed.

The bill provides an effective date of upon becoming a law, and it applies to property transfers in which the first transfer to an artificial entity occurs after the effective date.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

The Revenue Estimating Conference met April 17, 2008 and adopted an estimate that the bill would have a positive cash impact in fiscal year 2008-2009 of $30.1 million with a positive annualized impact of $50.2 million.

B. Private Sector Impact:

Certain transfers of property not subject to tax under the Department's current administration of Ch 201, F.S., as a result of the opinion announced by the Supreme Court opinion in *Crescent*, are again subject documentary stamp taxation under the bill.

C. Government Sector Impact:

Florida relies on documentary stamp tax revenue to fund the payment of debt service on a variety of environmental bond issuances as well as a variety of trust funded programs. State General Revenue receives a residual amount after other distributions set forth in statute.

The bill specifies that the election shall be made using a form to be developed by the Department of Revenue. The department may experience expenses related to the development of the form, although it is not anticipated that the expenses would be significant.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS by Finance and Tax on April 21, 2008:
The committee substitute adds a presumption that there is a purchaser when a transfer results in any increase in the value of an ownership interest in an entity and makes technical changes for clarity. The committee substitute removes language specifying that exemptions from the documentary stamp tax must be expressly provided for in chapter 201, F.S., and that, absent an exemption, the tax shall apply to all deeds or other documents that transfer an interest in real property. The committee substitute removes language that specifies that revenues received under the legislation shall be deposited into the "Sadowski Affordable Housing Trust Fund."

CS by Judiciary on April 8, 2008:
The committee substitute adds a provision specifying that tax revenues resulting from the changes made by the bill shall be deposited into the "Sadowski Affordable Housing Trust Fund."

B. Amendments:

None.