

**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.)

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Prepared By: The Professional Staff of the Committee on Judiciary

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BILL: CS/SB 1366

INTRODUCER: Judiciary Committee and Senator Gruters

SUBJECT: Trusts

DATE: February 13, 2020

REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Stallard	Cibula	JU	<b>Fav/CS</b>
2.			BI	
3.			RC	

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**Please see Section IX. for Additional Information:**

COMMITTEE SUBSTITUTE - Substantial Changes

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**I. Summary:**

CS/SB 1366 grants a trustee of a “grantor trust” sole discretion to use trust assets to pay the grantor/settlor’s taxes on trust income. A grantor trust is one in which the grantor retains certain rights or powers over the trust such that federal tax law treats the grantor and the trust as one entity, thus making the grantor tax-liable for trust income.

Under current law, a trustee may pay the grantor’s trust-income taxes only if the trust instrument authorizes it. Under the bill, the trustee generally may pay these taxes unless the trust instrument prohibits it or the trustee is:

- A beneficiary of the trust.
- Treated as the owner of part or all of the trust under federal or state tax law.
- A “related or subordinate party” with respect to:
  - A person treated as the owner of all or part of the trust under federal or state tax law; or
  - A beneficiary of the trust.

Moreover, the bill specifies that a life insurance policy held in the trust, the policy’s cash value, or a loan secured by the policy may not be used to pay the grantor’s income taxes.

Finally, the bill provides that it applies to trusts created before or after the effective date of the bill unless:

- The trustee gives the grantor and all others who may remove the trustee 60 days’ notice that the trustee intends to irrevocably opt out of the bill’s application to the trust; or

- Applying the bill would prevent a contribution to the trust from qualifying for, or would reduce, a federal tax benefit.

## II. Present Situation:

### Overview

When a grantor is required to pay federal income tax on income from a grantor trust, the trustee may pay these taxes for the grantor only if the trust instrument authorizes it.

### Trusts

A trust is a legal instrument, into which a “settlor” (or grantor) places property in the care of a “trustee,” who administers the property according to the terms of the trust for the benefit of one or more “beneficiaries.” For example, a father might place \$100,000 in trust for the benefit of his children, the proceeds to be used only for their education, and appoint the father’s certified financial planner as the trustee.

### Grantor Trusts

“Grantor trust” is a term commonly used to describe a trust for which the settlor (grantor) is also its “owner” under federal tax law.<sup>1</sup> Under this arrangement, the grantor and the trust<sup>2</sup> are treated as one entity under federal income tax law, thus requiring the settlor to pay income tax on income generated by the trust.<sup>3</sup>

Under sections 671-679 of the U.S. Internal Revenue Code, a grantor will be treated as the owner of a trust if the grantor retains certain rights to or powers over the trust, including:

- A reversionary interest that exceeded 5 percent of the value of the income or corpus at the trust’s inception;<sup>4</sup>
- The “power to control beneficial enjoyment” of the corpus or income *without* the approval of an “adverse party,” which is a person, such as a beneficiary, whose substantial interest in the trust will be adversely affected by the exercise of the power;<sup>5</sup>
- Certain “administrative powers,” such as the power to borrow from the corpus at low or no interest, or to sell the trust assets for below market value, without the approval of an adverse party;<sup>6</sup>
- The “power to revoke,” that is, the power to revest title to trust property in the grantor;<sup>7</sup> or
- The right to income for the grantor or spouse without approval of an adverse party.<sup>8</sup>

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<sup>1</sup> See 26 U.S.C. s. 671 (2020); *Sun First Nat. Bank of Orlando v. U.S.*, 607 F. 2d 1347 (U.S. Ct. of Claims 1979).

<sup>2</sup> A grantor may also “own” a *portion* of a trust’s assets. See *e.g.*, 26 U.S.C. s. 671 (2019).

<sup>3</sup> *Id.*

<sup>4</sup> 26 U.S.C. s. 673 (2020).

<sup>5</sup> 26 U.S.C. s. 674 (2020).

<sup>6</sup> 26 U.S.C. s. 675 (2020).

<sup>7</sup> 26 U.S.C. s. 676 (2020).

<sup>8</sup> 26 U.S.C. s. 677 (2020).

At some point, a given grantor might decide that the benefits of the grantor trust no longer outweigh the costs, which include the grantor's personal liability for the trust's income taxes. To address this issue, the trust could be converted to a nongrantor trust. However, this option has its disadvantages, such as potentially jeopardizing the trust's ability to own stock in an S corporation and subjecting the trust's income to higher income tax brackets.<sup>9</sup>

### **Legislation in Other States**

Several states, including Colorado,<sup>10</sup> Delaware,<sup>11</sup> New Hampshire,<sup>12</sup> and New York,<sup>13</sup> grant a trustee the discretion to pay a grantor's trust-income taxes unless the trust instrument expressly prohibits it.

### **III. Effect of Proposed Changes:**

The bill grants a trustee of a "grantor trust" sole discretion to use trust assets to pay the grantor/settlor's taxes on trust income. A grantor trust is one in which the grantor retains certain rights or powers over the trust such that federal tax law treats the grantor and the trust as one entity, thus making the grantor tax-liable for trust income.

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Moreover, the bill specifies that a life insurance policy held in the trust, the policy's cash value, or a loan secured by the policy may not be used to pay the grantor's income taxes.

Finally, the bill provides that it applies to trusts created before or after the effective date of the bill unless:

- The trustee gives the grantor and all others who may remove the trustee 60 days' notice that the trustee intends to irrevocably opt out of the bill's application to the trust; or
- Applying the bill would prevent a contribution to the trust from qualifying for, or would reduce, a federal tax benefit.

The bill takes effect July 1, 2020.

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<sup>9</sup> See 26 U.S.C. 1361(c)(2)(A)(i) (broadly permitting grantor trusts to be shareholders in S corporations, but permitting only certain types of other trusts to do the same).

<sup>10</sup> Colo. Rev. Stat. § 15-5-818 (2019).

<sup>11</sup> Del. Code 12 § 3344 (2019).

<sup>12</sup> N.H. Rev. Stat § 564-B:8-816(c) (2019).

<sup>13</sup> N.Y. Est. Powers and Trusts Law § 7-1.11(a) (2019).

**IV. Constitutional Issues:**

## A. Municipality/County Mandates Restrictions:

None.

## B. Public Records/Open Meetings Issues:

None.

## C. Trust Funds Restrictions:

None.

## D. State Tax or Fee Increases:

None.

## E. Other Constitutional Issues:

The bill states it is intended to be applied retroactively. Particularly, it provides that it applies to “all trusts, whether created on, before, or after July 1, 2020.”

The Florida Supreme Court has developed a two-prong analysis for determining whether a statute may be applied retroactively.<sup>14</sup> First, there must be “clear evidence of legislative intent to apply the statute retrospectively.”<sup>15</sup> If so, then the court moves to the second prong, “which is whether retroactive application is constitutionally permissible.”<sup>16</sup> Retroactive application is unconstitutional if it deprives a person of due process by impairing vested rights or imposing new obligations to previous conduct:

A retrospective provision of a legislative act is not necessarily invalid. It is so only in those cases wherein vested rights are adversely affected or destroyed or when a new obligation or duty is created or imposed, or an additional disability is established, on connection with transactions or considerations previously had or expiated.<sup>17</sup>

A court may determine that the bill negatively affects a vested right, such as a beneficiary’s right to receive income from a trust. This right could be diminished by the trustee’s payments from trust assets for the grantor’s income taxes. However, given how much authority a grantor has over a grantor trust, a court could find that a beneficiary in a given case had a mere expectancy interest, as opposed to a vested right, in trust assets that were used to pay a grantor’s income taxes.

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<sup>14</sup> See, e.g., *Florida Ins. Guar. Ass’n, Inc. v. Devon Neighborhood Ass’n, Inc.*, 67 So. 3d 187, 194 (Fla. 2011).

<sup>15</sup> *Metropolitan Dade County v. Chase Federal Housing Corp.*, 737 So. 3d 494 (Fla. 1999).

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* at 503 (citing *McCord v. Smith*, 43 So. 2d 704, 708-09 (Fla. 1949)).

**V. Fiscal Impact Statement:**

## A. Tax/Fee Issues:

None.

## B. Private Sector Impact:

None.

## C. Government Sector Impact:

None.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

**VIII. Statutes Affected:**

This bill creates section 736.08145 of the Florida Statutes.

**IX. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:  
(Summarizing differences between the Committee Substitute and the prior version of the bill.)**CS by Judiciary Committee on February 11, 2020:**

The committee substitute:

- Prohibits a trustee from choosing to pay the grantor's trust-income taxes if the trustee is a beneficiary or is a related or subordinate party to a beneficiary;
- Provides that if a trust advisor, protector, or other person is authorized to act in place of a trustee by the trust's terms, that person may also choose to pay the grantor's trust-income taxes; and
- Provides that the bill does not, of itself, make anyone a beneficiary of a trust, including for the purposes of determining the elective estate.

## B. Amendments:

None.