

HOUSE OF REPRESENTATIVES STAFF FINAL BILL ANALYSIS

BILL #: CS/HB 901 Secured Transactions
SPONSOR(S): Judiciary Committee, Fabricio and others
TIED BILLS: **IDEN./SIM. BILLS:** CS/SB 978

FINAL HOUSE FLOOR ACTION: 112 Y's 0 N's **GOVERNOR'S ACTION:** Approved

SUMMARY ANALYSIS

CS/HB 901 passed the House on April 20, 2023, as CS/SB 978.

A security interest arises when, in exchange for a loan, a borrower pledges as collateral in a security agreement specified assets he or she owns that the lender may take if the borrower defaults on the loan. A security interest also assures the lender that, if the borrower enters bankruptcy, the lender may be able to recover the loan's value by taking the asset. Under Florida law, a description of an asset, whether or not the description is specific, is sufficient to pledge the asset under a security agreement if it reasonably identifies what is described. However, a description of assets in general terms, such as "all the debtor's assets," "all the debtor's personal property," or similar phrasing, does not sufficiently identify the collateral for purposes of a security interest.

Florida law protects certain assets from legal process so that they remain out of a creditor's reach, including:

- Funds held in individual retirement accounts ("IRA") and other tax-exempt accounts.
- The cash surrender value of a life insurance policy and the proceeds of an annuity contract.
- Funds held in qualified tuition programs and medical, Coverdell education, and hurricane savings accounts.
- Disability income benefits.
- A deceased person's wages and unemployment compensation benefits.
- Homestead property and certain personal property items.
- Social security benefits; unemployment compensation, or public assistance benefits; veterans' benefits; alimony, support, or separate maintenance; and stock or pension plans under specified circumstances.

Historically, exempt assets not specifically pledged in a security agreement remained exempt from a creditor's reach. However, a recent Eleventh Circuit Court of Appeals decision broke with this rule by holding that a security agreement granting a security interest in "all assets and rights of the Pledgor" pledged the debtor's IRA as collateral for a loan even though the IRA was not specifically identified in the agreement. This decision may have significant federal tax consequences for Floridians, as the use of certain tax-exempt accounts as collateral for a loan is considered distribution of the funds to the owner, who then owes federal income tax on the money and may owe a tax penalty for early distribution.

The bill provides that a general description only by type of collateral is an insufficient description to pledge certain statutorily-exempt assets for the purposes of a security agreement.

The bill does not appear to have a fiscal impact on state or local governments.

The Governor approved the bill on June 20, 2023, ch. 2023-266, and it took effect on that date.

I. SUBSTANTIVE INFORMATION

A. EFFECT OF CHANGES:

Background

Security Interests

A security interest arises when, in exchange for a loan, a borrower pledges as collateral¹ in a security agreement² specified assets owned by the borrower that the lender may take if the borrower defaults on the loan.³ A security interest also assures the lender that, if the borrower enters bankruptcy, the lender may be able to recover the loan's value by taking possession of the pledged assets.⁴

Under Florida law, a description of personal or real property, whether or not it is specific, is sufficient for the purposes of a security agreement if it reasonably identifies what is described.⁵ An effective description of collateral pledged in a security agreement identifies the asset by:

- Specific listing;
- Category;
- Type of collateral;
- Quantity;
- Computational or allocational formula or procedure; or
- Any method under which the collateral's identity is objectively determinable.⁶

However, a general description of collateral as "all the debtor's assets," "all the debtor's personal property," or similar phraseology does not sufficiently identify the collateral for purposes of creating a security interest.⁷ Further, a description only by type of collateral is an insufficient description of:

- A commercial tort claim;
- In a consumer transaction, consumer goods, a security entitlement, a securities account, or a commodity account; or
- An account consisting of a right to payment of a monetary obligation for the sale of real property that is the debtor's homestead under Florida law.⁸

Asset Exemptions

Florida law protects certain assets from legal process so that they generally remain out of a creditor's reach, including:

- Funds held in an individual retirement account ("IRA") and other tax-exempt accounts.⁹
- A life insurance policy's proceeds.¹⁰
- A life insurance policy's cash surrender value.¹¹
- An annuity contract's proceeds.¹²

¹ "Collateral" means the property subject to a security interest. The term includes proceeds to which a security interest attaches; accounts, chattel paper, payment intangibles, and promissory notes that have been sold; and goods that are the subject of consignment. S. 679.1021(1)(l), F.S.

² "Security agreement" means an agreement that creates or provides for a security interest. S. 679.1021(1)(uuu), F.S.

³ Legal Information Institute, *Secured Transactions*, https://www.law.cornell.edu/wex/secured_transactions (last visited April 26, 2023).

⁴ *Id.*

⁵ S. 679.1081(1), F.S.

⁶ S. 679.1081(2), F.S.

⁷ S. 679.1081(3), F.S.

⁸ S. 679.1081(5), F.S.

⁹ S. 222.21, F.S.

¹⁰ S. 222.13, F.S.

¹¹ S. 222.14, F.S.

¹² *Id.*

- Funds held in qualified tuition programs, medical savings accounts, Coverdell education accounts, and hurricane savings accounts.¹³
- Disability income benefits.¹⁴
- A deceased person's wages, travel expenses, and reemployment assistance or unemployment compensation payments.¹⁵
- Homestead property.¹⁶
- Certain personal property items.¹⁷
- A debtor's interest in a motor vehicle, up to \$1,000 in value, and any professionally prescribed health aides.¹⁸
- Social security benefits; unemployment compensation, or public assistance benefits; veterans' benefits; alimony, support, or separate maintenance; and stock or pension plans under specified circumstances.¹⁹

The purpose behind such exemptions is to prevent a debtor from being left destitute, and therefore unable to participate productively in society, or from being unable to meet specified medical, educational, housing, and other needs, after defaulting on a loan or owing on a judgment.²⁰ Historically, exempt assets have remained exempt from a creditor's reach unless specifically pledged as collateral in a security agreement.²¹

Recent Case Law

In *Kearney Constr. Co., LLC v. Travelers Casualty & Surety Co. of America*, the federal Eleventh Circuit Court of Appeals broke with the historic tradition of maintaining asset exemptions unless the asset is specifically pledged.²² In *Kearney*, the debtor obtained a line of credit and pledged the following collateral in the security agreement:

[A]ll assets and rights of the Pledgor, wherever located, whether now owned or hereafter acquired or arising, and all proceeds and products thereof, all goods (including inventory, equipment and any accessories thereto), instruments (including promissory notes)[,] documents, accounts, chattel paper, deposit accounts, letters of credit, rights, securities and all other investment property, supporting obligation[s], and contract or contract rights or rights to the payment of money, insurance claims, and proceeds, and general intangibles.²³

The Court held that this language was an “unambiguous pledge” of “all assets and rights” of the debtor, including the debtor's IRA, even though the IRA was not specifically identified in the agreement.²⁴

¹³ S. 222.22, F.S.

¹⁴ S. 222.18, F.S.

¹⁵ Ss. 225.15 and 225.16, F.S.

¹⁶ Ss. 222.01-222.05, F.S.; Art. X, s. 4, Fla. Const.

¹⁷ S. 222.061, F.S.

¹⁸ S. 222.25, F.S.

¹⁹ Ss. 222.201 and 222.21(1), F.S.

²⁰ National Bankruptcy Review Commission, *Property Exemptions*, <https://govinfo.library.unt.edu/nbrcreport/05ccons.html> (last visited April 26, 2023).

²¹ Real Property, Probate, and Trust Law Section of the Florida Bar (“RPPTL”), *White Paper* (Jan. 26, 2021); see, e.g., *Havoco of Am. Ltd. v. Hill*, 790 So. 2d 1018 (Fla. 2001); *Connor v. Seaside Nat'l Bank*, 135 So. 3d 508 (Fla. 5th DCA 2014); *Killian v. Lawson*, 387 So. 2d 960 (Fla. 1980).

²² See 795 Fed. Appx. 671 (11th Cir. 2019). The *Kearney* case is an unpublished opinion of the Federal Court of Appeals for the Eleventh Circuit. Opinions that the Eleventh Circuit's panel of judges believes to have no precedential value are not published. Although unpublished opinions maybe cited as persuasive authority, they are not considered binding precedent. Fed. Re. App. P. 36, Internal Operating Procedure 6; see also 11th Cir. R. 36-2.

²³ 795 Fed. Appx. at 673-74.

²⁴ *Id.* at 674. The borrower testified that he did not intend to pledge the IRA; however, the lower court rejected such testimony because it was inconsistent with the borrower's earlier court filings. *Id.*

Practically speaking, the *Kearney* decision makes it possible for a borrower to inadvertently pledge as collateral for a security agreement an asset historically exempt from the reach of creditors under Florida law.²⁵ This may affect Florida consumers with security agreements containing general language similar to the language at issue in *Kearney*.

The decision could also have significant federal tax implications, as the use of certain tax-exempt accounts as collateral for a loan is considered a distribution of the funds in the account to the owner, who then may owe federal income tax on the distribution.²⁶ The Tax Code also imposes a 10 percent tax penalty for early distributions from certain tax-exempt accounts.²⁷

Effect of the Bill

The bill provides that a general description only by type of collateral is an insufficient description to pledge as collateral, for the purposes of a security agreement, accounts and other entitlements set forth in ss. 222.13-222.16, 222.18, and 222.201-222.22, F.S. These include:

- Funds held in an IRA and other tax-exempt accounts.
- A life insurance policy's proceeds or cash surrender value.
- An annuity contract's proceeds.
- Funds held in qualified tuition programs, medical savings accounts, Coverdell education accounts, and hurricane savings accounts.
- Disability income benefits.
- A deceased person's wages, travel expenses, and reemployment assistance or unemployment compensation payments.
- Social security benefits; unemployment compensation; public assistance benefits; veterans' benefits; alimony, support, or separate maintenance; and stock or pension plans under specified circumstances.

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II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

²⁵ The exception is homestead property, as a waiver of such rights must be "knowing, voluntary, and intelligent" to have any effect. See RPPTL, *supra* note 21; see also *Chames v. DeMayo*, 972 So. 2d 850 (Fla. 2007) (citing *State v. Upton*, 658 So. 2d 86 (Fla. 1995)).

²⁶ I.R.C. 408(e)(4) and (d)(1); I.R.C. 72(p)(1)(B).

²⁷ I.R.C. 72(t).

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill may prevent Floridians from inadvertently pledging as security specified exempt assets and suffering any related federal tax consequences.

D. FISCAL COMMENTS:

None.