



Florida's Unlimited Homestead Exemption Does Have *Some* Limits

Part I

by Barry A. Nelson and Kevin E. Packman

In recent articles discussing high-profile corporate malfeasance and accounting scandals, the use of Florida's unlimited homestead exemption to avoid creditors' claims has been noted with concern.¹ Often referring to it as a legal loophole, detractors of the unlimited homestead exemption point out that the exemption permits debtors to divert substantial assets to the purchase of new and extravagant homes that can be shielded from creditors under Florida's state constitution. *The Washington Post*,² on July 12, 2002, reported that Scott D. Sullivan, former CFO of WorldCom, is building a \$15 million Boca Raton "mansion" that may qualify for homestead exemption status. Yet, concerns about Florida homestead detailed in the national press are nothing new. For example, in 1991, *The New York Times* reported that Bowie Kuhn, the former Major League Baseball Commissioner, had sold his \$1.2 million New Jersey home and within weeks had bought a similar estate in Florida to shield his assets before then filing for bankruptcy.³ These and many other articles express concern that debtors can avoid creditors by moving to Florida, purchasing a new home and establishing residency.

While some may benefit from such planning, many debtors, as well as reporters writing about them, are unaware of the requirements that must be satisfied to obtain the benefits of Florida's homestead exemption. This article will discuss the limits of Florida's exist-

The homestead exemption is deceptively simple on its face. In the real world, differing facts can produce dramatically different results.

ing homestead exemption for asset protection. As such, Part I of this article will focus on the exemption provided by the Florida Constitution in Art. X, §4 and its legislative implementation by the F.S. ch. 222. It will not discuss Florida's homestead exemption for purposes of ad valorem taxation, which is found in the F.S. ch. 196.

In Part II, the article will discuss certain federal limitations on the homestead exemption (such as federal tax liens), fraudulent transfer issues and proposed federal bankruptcy legislation that would severely limit homestead protection for non-Florida debtors seeking to establish domicile and move to Florida to avoid creditors. In addition, Part II will discuss planning to take advantage of homestead and conflicts that can arise in that context between professional advisors

who may have different views. Some advisors may recommend owning a homestead with little mortgage debt, while others may recommend owning the homestead with a significant mortgage in order to benefit from mortgage interest deductions for federal income tax purposes and from the ability to enhance other investments through funds that are not tied up in home equity. While there may be merit from a financial and tax standpoint to place a large mortgage on a homestead, those concerned with asset protection may find that having no mortgage, or a small mortgage, on their homestead provides peace of mind that is more important than the tax and financial advantages.

Florida Constitution

Art. X, §4 of the Florida Constitution sets forth the homestead exemption. It states:

(a) There shall be exempt from forced sale under process of any court, and no judgment, decree or execution shall be a lien thereon, except for the payment of taxes and assessments thereon, obligations contracted for the purchase, improvement or repair thereof, or obligations contracted for house, field or other labor performed on the realty, the following property owned by a natural person:

(1) a homestead, if located outside a municipality, to the extent of 160 acres of contiguous land and improvements thereon, which shall not be reduced without the owner's consent by reason of subsequent inclusion in a municipality; or if located within a municipality, to the extent of one-half acre of contiguous land, upon which the exemption shall be limited to the residence of the owner or the owner's family.

There are thus three significant requirements that the courts must consider in order to determine whether a debtor's homestead qualifies for Florida's constitutional exemption from forced sale: (1) acreage limitations, (2) residency requirements and (3) ownership requirements. Of course, to be eligible for protection from creditors, the property must be located in the State of Florida.⁴ Furthermore, for policy reasons, homestead laws are applied liberally in favor of the homeowner.

Policy Behind the Homestead Exemption

Because the purpose of the unlimited exemption is to protect families from misfortune, the burden is on the creditor to argue against homestead protection.⁵ In *Public Health Trust v. Lopez*, 531 So. 2d, 946, 948 (Fla. 1988), *aff'g*, 509 So. 2d 1286 (Fla. 3d DCA 1987), the court stated that the purpose of the homestead law is to promote the stability and welfare of the state by securing to the householder a home, so that the homeowner may live beyond the reach of financial misfortune. Similarly, in *Orange Brevard Plumbing & Heating Co. v. La Croix*, 137 So. 2d 201, 204 (Fla. 1962), the court said that the purpose of the homestead law "is to benefit the debtor by securing his or her homestead beyond all liability from forced sale under process of any court." Such cases reflect that courts apply the homestead exemption laws liberally so that families will have shelter and will not be reduced to absolute destitution.

Acreage Limitations

Whether the residence is within or without a municipality is of critical importance in determining the portion of the debtor's homestead that will be protected. As stated above, Florida's constitutional protection is generally limited to the extent of one-half acre if the residence is within a municipality. Until 1997 when the U.S. Supreme Court denied cert in the case *In re Englander*, 520 U.S. 1186 (1997), thereby letting stand the decision of

the 11th Circuit Court of Appeals,⁶ the extent to which homestead protection was available for a residence on more than one-half acre within a municipality was uncertain.⁷

The debtor in *Englander* owned a home on approximately one acre within a municipality, and the property could not be legally subdivided due to local zoning regulations. The debtor claimed a homestead exemption for a portion of the property that surrounded the non-exempt portion, eliminating any reasonable access to the nonexempt portion and rendering it valueless. The court, in reaching its conclusion that the homestead designation sought for a portion of the property was improper, stated that the debtor's "attempt at homestead exemption 'germymandering' was clearly in bad faith."⁸ The bankruptcy court granted the debtor an exemption in a portion of the proceeds to be derived from the sale of the property equal to the value of one-half acre.⁹ The Court of Appeals reasoned that a sale and apportionment of the sales proceeds is an equitable solution that allows for the appropriate recognition of the debtor's homestead and affords creditors some satisfaction of their claims.

The 11th Circuit Court of Appeals reinforced *Englander* when given an opportunity *In re Kellogg*, 197 F.3d 1116 (1999). There, the debtor, who owned a 1.3 acre oceanfront home in Palm Beach, argued his home should not be sold to pay creditors. Instead, the debtor reasoned, he should be able to remain in his residence and surrounding property to the extent of one-half acre; the remaining acreage could be assigned to creditors. The court found that Palm Beach's zoning laws required a minimum parcel size that could not be maintained after subdivision. As a result, relying on *Englander*, the court ordered the sale of the homestead property and an allocation of the proceeds, with the proceeds which exceeded those attributable to one-half acre being made available to creditors.

As shown by the *Englander* and *Kellogg* decisions, courts can order

the sale of a homestead when such property exceeds the constitutional size limitations set forth in the Florida Constitution, and when the property cannot be practically or legally subdivided. Consequently, it may be advisable for individuals concerned about retaining protection for all of their homestead real estate to either purchase a residence outside a municipality on 160 acres or less or to purchase a residence within a municipality located on no more than one-half acre. Alternatively, a would-be debtor could purchase a condominium, which could be fully protected by the exemption.

As noted above, Art. X, §4(a)(1) of Florida's Constitution provides that the acreage limitation may not be reduced without the owner's consent by reason of subsequent inclusion in a municipality. Thus, assuming the size of the homestead does not exceed 160 acres, homeowners need not be concerned whether they will lose their homestead protection if they live in a home that exceeds one-half acre within an unincorporated area that later becomes a municipality. For example, four municipalities in South Florida have incorporated since 1990: Aventura, Key Biscayne, Pinecrest and Sunny Isles Beach. Persons owning homes in these or other new municipalities on more than one-half acre (but on no more than 160 acres) *before* the date of the municipal incorporation will continue to benefit from the 160-acre limitation for as long as their homes continue as their homestead. Accordingly, certain homes within new municipalities are effectively "grandfathered" for homestead protection while those purchased after becoming a municipality are subject to the usual one-half acre limitation. This distinction causes a potential trap for those advisors who simply apply the one-half acre rule without questioning the date of incorporation of a municipality and the date that home was purchased.

Residence Limitations

To obtain the benefits of the homestead exemption for asset pro-

tection the debtor must be a resident in Florida. In order to be a resident of Florida, the debtor must have a residence in the state as well as the actual intent to reside in Florida permanently.¹⁰ An alien debtor can only satisfy the permanent residency requirement if the debtor is granted a permanent visa or "green card."¹¹ The bankruptcy court in *In re Bermudez*, 1992 Bankr. LEXIS 547, at *4 (Bankr. S.D.Fla. 1992), citing *In re Gilman*, 68 Bankr. 374, 375-376 (Bankr. S.D.Fla. 1986), and *In re Cooke*, 412 So. 2d 340, 342 (Fla. 1982), reasoned that "unless the debtor is issued such permanent status, the alien debtor cannot legally formulate the requisite intent to make the house the family's permanent residence, regardless of the debtor's subjective intention to remain indefinitely." Accordingly, in *In re Boone*, 134 B.R. 979 (Bankr. M.D. Fla. 1991), the bankruptcy court held that a noncitizen of the U.S., who had failed to maintain her U.S. visa status and had lost the right to remain in the U.S. at the time she filed for bankruptcy, was not a resident of Florida for purposes of the homestead forced sale exemption.

If the court finds that the owner of an otherwise qualified homestead has formed the requisite intent to obtain a homestead in Florida, the results can be quite advantageous for debtors who are new Florida residents if another potential obstacle is overcome. Under existing bankruptcy laws, prior to obtaining creditor protection, debtors must be Florida residents or domiciliaries for the greater portion of the 180 days prior to filing for federal bankruptcy protection.¹² F.S. §222.17 instructs individuals on how to establish domicile for purposes of being eligible for the homestead exemption. It states that any person who has a domicile in Florida simply needs to file a sworn statement with the clerk of the county in which such person resides stating that "he or she resides in and maintains a place of abode in that county which he or she recognizes and intends as his or her permanent home."¹³ If the individual also has a domicile in another

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state, the sworn statement must indicate that "his or her place of abode in Florida constitutes his or her predominant and principal home, and that he or she intends to continue it permanently as such."¹⁴ Under Florida law, "where a good faith intention is coupled with an actual removal evidenced by positive overt acts, then the change of residence is accomplished and becomes effective."¹⁵ However, even if such a statement is filed, unless a person actually spends more time in Florida than elsewhere and holds himself or herself out as a Florida resident, the statement by itself is likely to have no benefit to establishing such person's Florida domicile.¹⁶ F.S. §222.01 provides a form for notice of homestead that responds to a certified judgment filed in the public records. The notice of homestead states the property is homestead and that the judgment does not contain a valid lien and provides 45 days for the holder of the judgment to file a claim for a declaratory judgment to determine the constitutional homestead status of the property.

Assuming the residency/domiciliary requirement is satisfied, separated married couples may find themselves in the situation of benefiting from two homestead exemptions. The U.S. Court of Appeals in *In re Colwell*, 196 F.3d 1225 (11th Cir. 1999) held that a married couple living in separate residences

for over three years prior to the filing of their respective bankruptcy petitions qualified for homestead protection for each residence because there was no showing of fraudulent intent behind their marital separation. Similarly, a bankruptcy court held that, after a separation by two spouses, each would be able to claim a homestead in a home even though the net effect would be to exempt two homesteads where both had filed separate bankruptcies.¹⁷

Ownership Requirements

Once debtors have established a Florida residence on the requisite acreage, in order to obtain protection they must also meet ownership requirements. The identity of the legal owner of the homestead can have dramatic impact on the availability of the exemption. In a December 2001 decision that is likely to be controversial, the bankruptcy court held a debtor could *not* claim the homestead exemption from forced sale for a personal residence she owned not in her individual capacity, but as trustee of the revocable trust into which she had conveyed the homestead. *Crews v. Bosonetto (In re Bosonetto)*, 271 B.R. 403 (Bankr. M.D. Fla. 2001). The court in *Bosonetto* reasoned the homestead exemption from forced sale can only be claimed for property owned by a natural person. If homestead protection for asset protection purposes is an objective, the safest manner in which to hold title is in an individual capacity or as tenants by the entirety for a husband and wife, and not through a trust, corporation, partnership, LLC, or other business entity.

Kinds of Residence Qualifying as Homestead

The types of residence that have been found to qualify as homestead are countless. Further, the interest in the underlying homestead can be fractional,¹⁸ a leasehold,¹⁹ or a share in a co-operative apartment.²⁰ In a March 2002 Florida district court of appeal decision, the court stated, "Although a castle to one person

may be a shanty to another, the law does not so discriminate. Thus, regardless of whether one's castle is a traditional family home or a modest cottage, whether it is a rural farmhouse or a villa by the sea, whether it floats or sits on wheels, whether it is a condominium or a cop, it should receive the same protection under Florida law."²¹

Courts and legislation have extended the protection of homestead from forced sale to include many locations beyond the typical home. F.S. Ch. 222 is the legislature's implementation of Florida's constitutional protection against the forced sale of homestead. Section 222.05 provides:

[a]ny person owning and occupying any dwelling house, including a mobile home used as a residence, or modular home, on land not his or her own which he or she may lawfully possess, by lease or otherwise, and claiming such house, mobile home, or modular home as his or her homestead, shall be entitled to the exemption of such house, mobile home, or modular home from levy and sale as aforesaid.

Thus, homestead may be claimed by debtors for structures in which they have an ownership interest even though the debtors do not own the property on which the structure is situated. As such, courts have held that motor coaches, travel trailers and even motorboats could, under the proper factual circumstances, be found to have the requisite permanence to qualify for the homestead exemption. *In re Bubnak*, 176 B.R. 601 (Bankr. M.D. Fla. 1994), the court held that a motor coach qualified as a homestead since it was the debtor's permanent residence and was permanently hooked up to utilities. Similarly, in *In re Meola*, 158 B.R. 881 (Bankr. S.D. Fla. 1993), the court found that a travel trailer qualified as the debtor's homestead and, thus, the debtor could benefit from the homestead exemption. Note, however, that when the debtor owns the land upon which a mobile home is located, §222.05 is not applicable, and both the land and mobile home qualify as homestead.²²

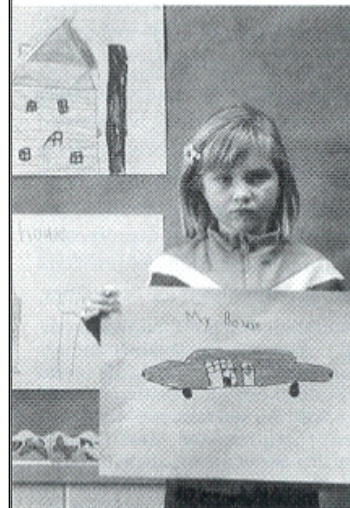
Decisions are in conflict as to whether motorboats can qualify for homestead protection. For example,

in *In re Mead*, 255 B.R. 80 (Bankr. S.D. Fla. 2000), the court, seeing "no distinction between a mobile home occupying leased space in a mobile home park, and a boat occupying leased dock space in a marina or in another dockage situation," permitted a debtor to claim a homestead in his 34-foot cabin cruiser. Several other courts have reasoned to the contrary that "a debtor cannot transform a movable chattel into a homestead by choosing to leave the chattel in one place or by failing to maintain the chattel in a movable condition."²³ Consistent with this approach, the court in *In re Hacker*, 260 B.R. 542, 546 (Bankr. M.D. Fla. 2000), gave no weight to the fact that the debtor's 34-foot boat was 1) docked at a marina, 2) hooked up both to water and electricity from land, and 3) contained a broken engine that the debtors could not afford to fix, reasoning that "the potential mobility of the boat alone negates the permanency required for the homestead exemption."²⁴

Occupancy Prerequisite to Homestead Status

Despite contrary statements in recent newspaper articles,²⁵ a majority of the courts have ruled that neither a home under construction nor a vacant lot is eligible for the homestead exemption from forced sale. This issue appears to have been settled in the 1882 case of *Drucker v. Rothstein*, 19 Fla. 191 (1882), where the court held that a parcel of land, never occupied as a dwelling place or home, and incapable of such occupancy, is not a homestead under the Florida Constitution. The *Drucker* opinion stated "A bare lot unoccupied cannot be a homestead. Lumber placed upon it for the purpose of building is not such occupancy, even though there may be a contract made for building."²⁶ Similarly, in a more recent case, a lot which had never been lived on was found ineligible for homestead protection. In *In re Estate of Ritter*, 407 So. 2d 386 (Fla. 3d DCA 1981), a vacant lot owned by the debtor and adjoining his homestead was found not to be part of the

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debtor's homestead residence. The court reasoned "[the lot] at no time had any structures or improvements built upon it which served the residence ... and was never jointly fenced in with the [residence]. It was merely a separate, empty lot which served, at best, as an excess side yard to the aforementioned residence."²⁷

It appears that actual occupancy on the property for which homestead status is desired is a prerequisite to a court granting the property such character.²⁸ However, precedent may exist to allow homestead protection in very limited situations where property is being prepared for occupancy.

Where it is clearly the manifest intention of the owner to occupy the premises immediately as a home, and this intention is evidenced by specific acts and doings that are not compatible with a different intention, and there is nothing done by the claimant showing a different intention, or that is inconsistent with the asserted intention to make the place his homestead, the homestead character will attach.²⁹

In spite of the apparent weight to be given to a debtor's "manifest intention" to occupy a home, the authors have not located any Florida case granting homestead status to a debtor prior to the debtor's occupancy on the property.³⁰ For example, in *Wechsler v. Carrington*, 214 F. Supp.2d 1348 (S.D. Fla. 2002), a case decided more than 100 years after *Drucker*, the debtor purchased a condominium on August 31, 2001, and began moving property into the condominium in September 2001. However, the debtor continued to live in his rented apartment through January 2002. A foreign judgment was filed in Miami-Dade County on December 4, 2001, and the debtor filed for homestead exemption for the condominium on January 2, 2002. In denying homestead protection, the court reasoned that the debtor's actions were inconsistent with one preparing to move into a new homestead. Among such actions leading this court to its conclusion were: 1) the debtor's registering for a voter's registration card and driver's license in October 2001 at the rental address; 2) the fact that the debtor had two telephone lines and a cable modem at the rented

address and none at the condominium; and 3) the fact that on December 7, 2001, the debtor listed the rented address with SunTrust Bank upon opening two accounts.³¹ The debtor did not change his address for his voters registration or drivers license until January 31, 2002. The debtor also did not apply for homestead for property tax purposes until January 2, 2002, a few days after the Pennsylvania judgment was registered.

On the other hand, once a home obtains "homestead" status it remains homestead until it is abandoned. The debtor's failure to continue to occupy the residence he or she occupied at the time of judgment is not necessarily equivalent to abandonment and, thus, will not necessarily cause the homestead to lose its protected status. The general rule appears to be that if a debtor leaves his home due to financial, health or family reasons the debtor will not be considered to have abandoned the homestead. For example, *In re Herr*, 197 B.R. 939 (Bankr. S.D.Fla. 1996), the court noted the following do not necessarily constitute abandonment: 1) mere absence from the homestead for financial reasons; 2) posting a "for sale" or offering the property for sale; or 3) failing to maintain the property for extended periods.³² Similarly, homestead status is not lost when a debtor leaves the home with no intention of returning but has a good faith intent to reinvest the proceeds of a future sale of the house in a new homestead.³³ However, in *Dep't of Revenue ex rel. Vickers v. Pelsey*, 779 So. 2d 629 (Fla. 1st DCA 2001), funds that a debtor received from a commercial lender and which were intended to be used to acquire homestead were not protected under the homestead exemption. The court noted that no sale of a homestead was involved and, further, that the property mortgaged to secure the loan was also not homestead.³⁴

Part I Summary

In this part of the article, we have focused on the homestead exemp-

tion provided by the Florida Constitution in Art. X, §4 and its legislative implementation by the F.S. Ch. 222. As such, we discussed the policy behind the exemption, the limits on its use, namely the types of residences which may qualify as homestead, the size of limitations of the real property on which the homestead is situated and, finally, the manner in which residences, must be owned in order to qualify for homestead. The homestead exemption is deceptively simple on its face. In the real world, differing facts can produce dramatically different results, and debtors and their advisors must be sensitive to the nuances of the exemptions.

Next month, in Part II, we will discuss further limitations on the homestead exemption and proposed federal bankruptcy legislation that would severely limit homestead protection for those debtors seeking to move to Florida to avoid creditors. We will also discuss planning issues for homestead and potential conflicts that can arise between the attorney, CPA and financial planner when providing advice on homestead exemption planning. □

¹Jon Swartz, *Sullivan Estate Might Not be Exempt*, USA TODAY, August 13, 2002; Howard Goodman, *As WorldCom Workers Fret, Ex-CFO's Xanadu Rises*, FT. LAUDERDALE SUN-SENTINEL, July 25, 2002; Jon Swartz, *Homes of the Rich and Infamous*, USA TODAY, July 15, 2002; Philip Shenon, *Law Professors Express Concern Over Pending Bankruptcy Bill*, THE NEW YORK TIMES, May 22, 2002; Craig Gilbert, *Kohn Deal Tightens "Luxury Loophole"*, MILWAUKEE JOURNAL SENTINEL, April 24, 2002.

²Jackie Spinner, *Homes Remain Rogue Executives' Castles Under Loophole*, THE WASHINGTON POST.

³Murray Chass, *Kuhn's Descent from Commissioner to Legal Outcast*, THE NEW YORK TIMES, May 12, 1991, §8; p. 3, col. 1. See also, David Margolick, *Bowie Kuhn is Said to Be In Hiding*, THE NEW YORK TIMES, February 9, 1990, §D; p. 1, col. 6.

⁴*In re Sanders*, 72 B.R. 124, 125 (Bankr. M.D.Fla. 1987).

⁵*Lewton v. Hower*, 18 Fla. 872, 882 (Fla. 1882); *Graham v. Azar*, 204 So. 2d 193, 195 (Fla. 1967); *In re Haning*, 252 B.R. 799, 806 (Bankr. M.D.Fla. 2000) citing *In re Ehnle*, 124 B.R. 361, 363 (Bankr. M.D. Fla. 1991) ("placing the burden on objecting party to establish with preponderance of evidence that

debtors are not entitled to claimed exemption”).

⁶*Englander v. Mills (In re Englander)*, 95 F.3d 1028 (11th Cir. 1996). See also *In re Nofsinger*, 221 B.R. 1018 (Bankr. S.D.Fla. 1998), following *Englander*, which provided the parties 30 days from the order to submit an agreed order as to the value of the property that was not protected by homestead and the manner in which said amount was to be paid to the Bankruptcy Trustee for inclusion in the debtor’s bankruptcy estate. Otherwise, the trustee was authorized to sell the homestead (as set forth in *Englander*) and “the Court will apportion the proceeds accordingly.” *Id.* at 1021.

⁷Several Florida bankruptcy courts found that when the homestead property is not divisible, the trustee could sell the property and the court would apportion the proceeds. *In re Wierschem*, 152 B.R. 345, 347 (Bankr. M.D.Fla. 1993); *In re Baxt*, 188 B.R. 322, 323-324 (Bankr. S.D. Fla. 1995). Reflecting a contrary view, a court found that when the homestead was divisible, but the zoning laws prevented a sale, that the entire property would be exempt homestead. *In re Kuver*, 70 B.R. 192 (Bankr. S.D.Fla. 1986). Similarly, the Florida Supreme Court ordered the division and sale of property when a portion of the property was not being used as homestead. *Smith v. Guckenheimer*, 42 Fla. 1, 19 (Fla. 1900).

⁸*In re Englander*, 156 B.R. 862, 864 (Bankr. M.D.Fla. 1992).

⁹*Id.* at 870.

¹⁰*Hillsborough Inv. Co. v. Wilcox*, 13 So. 2d 448, 452 (Fla. 1943); *In re Cooke*, 412 So. 2d 340, 342 (Fla. 1982).

¹¹*In re Bermudez*, 1992 Bankr. LEXIS 547, at *4 (Bankr. S.D. Fla. 1992); *Raheb v. DiBattisto*, 513 So. 2d 717 (Fla. 3d D.C.A. 1987).

¹²*In re Whitehead*, 278 B.R. 597 (Bankr. M.D. Fla. 2002)(citing 11 U.S.C. §522(b)(2)(A) for the proposition that the ultimate fact to be determined in a bankruptcy proceeding was whether debtor had been “a bona fide resident or domiciled in the State of Florida for the 180-days immediately preceding the date of the filing of the Petition, or for the longer portion of such 180 day period than in any other place”); *In re Levy*, 221 B.R. 559, 567 (Bankr. S.D. Fla. 1998) (“under §522(b), the lack of a domicile in any state within the 180-day period immediately preceding the filing of the petition is fatal to any right of exemption under the laws of the state); *In re Dixon*, 153 B.R. 594 (Bankr. M.D. Fla. 1993) (reversed on other grounds). *But note*, the 2002 Bankruptcy Reform Bill discussed in Part II of this article, *infra*, if passed, will supersede this analysis and replace it with a 40-month residency requirement prior to filing for bankruptcy in order to obtain homestead benefits of the new domicile state.

¹³FLA. STAT. §222.17(1).

¹⁴FLA. STAT. §222.17(2).

¹⁵*Bloomfield v. St. Petersburg Beach*, 82 So. 2d 364, 368 (Fla. 1955).

¹⁶See, John K. Harris, Jr., *Practitioner’s Notes: Essentials of Estate Planning for the Professional Athlete*, 11 U. MIAMI ENT. & SPORTS L. REV. 159, 160-162 (1993) for a discussion on activities which can help establish a new domicile such as, but not limited to, obtaining a drivers license and voters registration card, filing income tax returns and paying tax in the domicile of choice; *Wells v. Vallier*, 773 So. 2d 1197 (Fla. 2d D.C.A. 2000) (where the court analyzed the taxpayers Florida contacts to determine whether they should be considered permanent residents of Florida despite having received a residency-based property tax credit in New Hampshire).

¹⁷*In re Russell*, 60 B.R. 190 (Bankr. M.D. Fla. 1986).

¹⁸*Vandiver v. Vincent*, 139 So. 2d 704 (Fla. 2^d D.C.A. 1962).

¹⁹*In re McAtee*, 154 B.R. 346, 349 (Bankr. N.D. Fla. 1993) (holding a 99-year lease was an ownership interest sufficient to satisfy the requirements of Florida’s homestead exemption to forced sale).

²⁰*In re Dean*, 177 B.R. 727 (Bankr. S.D. Fla. 1995).

²¹*S. Walls, Inc. v. Stilwell Corp.*, 810 So. 2d 566, 571 (Fla. 5th D.C.A. 2002).

²²“[I]t is unlikely that the legislature would provide protection for mobile homes on leased premises if similar protection were not already available to mobile homes on premises owned by the debtor.” *Gold v. Schwartz*, 774 So. 2d 879 (Fla. 4th D.C.A. 2001).

²³*In re Hacker*, 260 B.R. 542, 546 (Bankr. M.D. Fla. 2000) citing *In re Walter*, 230 B.R. 200, 203 (Bankr. S.D. Fla. 1999).

²⁴See *Hacker*, 260 B.R. at 546 quoting *In re Major*, 166 B.R. 457, 459 (Bankr. M.D. Fla. 1994).

²⁵See *supra*, note 1.

²⁶*Drucker*, 19 Fla. 191 at *5.

²⁷*Ritter*, 407 So. 2d at 387.

²⁸*Semple v. Semple*, 82 Fla. 138 (Fla. 1921) quoting *Solary v. Hewlett*, 18 Fla. 756 (Fla. 1882) (“Under our statute there is an unbroken series of decisions, that occupancy, the use of the house by the family as a homestead, are essential requirements to impress the property with the character of a homestead. A mere intention to occupy it, though subsequently carried out, is not sufficient.”); *Wechsler v. Carrington*, 214 F. Supp.2d 1348 (S.D. Fla. 2002) (following *Semple* and holding that a condominium was not homestead until after a Pennsylvania judgment was registered with the Florida court because before then the debtor did not actually use and occupy the property. The court stated that if a judgment is recorded prior to the time the debtor established homestead the property is subject to lien under Florida law); *Perez v. Marti*, 770 So. 2d 284, 290 (Fla. 3d D.C.A. 2000) citing *Keveloh v. Carter*, 699 So. 2d 285 (Fla. 5th D.C.A. 1997) (“change of residence is accomplished and becomes effective when there is a good faith intention to estab-

lish it, coupled with the actual physical move to a new residence, as evidenced by positive overt acts”).

²⁹*Semple*, 82 Fla. at 142 quoting *Oliver v. Snowden*, 18 Fla. 823 (Fla. 1882).

³⁰In each of the three cases that discuss the possibility of obtaining homestead exemption without occupying the land, the debtors were unsuccessful in their attempt to obtain a homestead exemption. In *Drucker*, lumber placed on the property was insufficient; in *Hewlett*, the debtor’s renting three houses on a plot of land he owned to tenants while saving money to renovate the houses into one large homestead was insufficient; and in *Snowden*, a plot of land the debtor and his family cultivated but upon which they did not live, was insufficient for homestead exemption.

³¹*Id.*

³²*Id.*

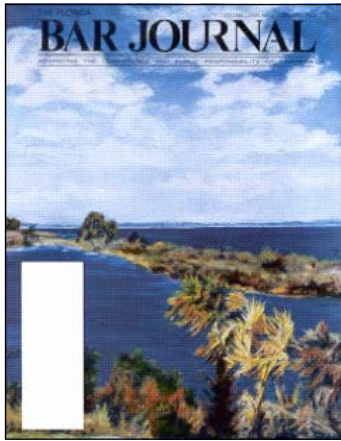
³³*La Croix*, 137 So. 2d at 204 (holding “only so much of the proceeds of the sale as are intended to be reinvested in another homestead may be exempt ... in order to satisfy the requirements of the exemption the funds must not be commingled with other monies of the vendor but must be kept separate and apart and held for the sole purpose of acquiring another home...[P]roceeds of the sale are not exempt if they are not reinvested in another homestead in a reasonable time or if they are held for the general purpose of the vendor.”)

³⁴*Pelsey*, 779 So. 2d at 633. See also *In re Lusiak*, 247 B.R. 699 (Bankr. N.D. Ohio 2000) (holding that because debtor’s bankruptcy petition and related documents stated debtors domicile to be in one state, debtor could not claim the homestead exemption of another state even if debtor had an intent to return to the state where her residence was located.)

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This column is submitted on behalf of the Real Property, Probate and Trust Law Section, Steven L. Hearn, chair, and Richard R. Gans and William P. Sklar, editors.



Florida's Unlimited Homestead Exemption Does Have *Some* Limits

Part II

by Barry A. Nelson and Kevin E. Packman

Last month in Part I of this article, we discussed how recent commentators discussing high-profile corporate malfeasance and accounting scandals have sometimes inaccurately reported the effectiveness with which executives (and, by association, debtors in general) can use Florida's unlimited homestead exemption to avoid creditors' claims under existing law. We focused on the exemption provided by the Florida Constitution in Art. X, §4 and its legislative implementation by the F.S. Ch. 222. We discussed the policy behind the homestead creditor's claim exemption, the types of residences that qualify as homestead, the size limitations of the real property on which the homestead is situated, and, finally, the manner in which a residence must be owned in order to qualify for homestead protection.

In Part II, we will discuss further state and federal law limitations on the homestead exemption, and proposed federal bankruptcy legislation which, if enacted, would severely limit homestead protection for those debtors seeking to move to Florida to avoid creditors. We will also discuss planning issues for homestead and potential conflicts that can arise between the attorney, CPA, and financial planner when providing advice on homestead exempt planning.

Limitations on Florida's Homestead Exemption Imposed by Federal Tax Law

In some cases federal tax law will

While there are many other asset protection techniques effective in Florida, it is the authors' opinion that the best protection planning is a diversified approach considering the exemptions of all options.

preempt Florida's homestead exemption. In 1998, the Bankruptcy Court held that a federal tax lien was enforceable against homestead property.¹ The Court found that "the homestead exemption does not erect a barrier around a taxpayer's home sturdy enough to keep out the Commissioner of the Internal Revenue."² However, due to Congress' concern that seizure of a taxpayer's principal residence is particularly disruptive for the taxpayer and the taxpayer's family, a taxpayer's principal residence may be seized to satisfy a taxpayer's tax liability only as a last resort. Further, the taxpayer's residence is exempt from levy unless a judge or magistrate of a U.S. district court approves the

levy in writing. See 26 U.S.C. §6334(a)(13)(B) and (e) (2002).

The Supremacy Clause of the U.S. Constitution is another avenue available to federal courts when seeking to preempt state law. U.S. Const. Art. VI. Preemption is authorized if:

Congress expressly provides for preemption, if the area of law is one of comprehensive federal regulation that leaves no room for state laws to supplement, if the state law affects a field of dominant federal interest precluding state laws on the same subject, or if the state law and the federal law are in actual conflict so that compliance with both is physically impossible or the state law obstructs the accomplishment of the full objectives of Congress.³

Accordingly, the 11th Circuit held that a federal civil forfeiture statute preempts the Florida homestead exemption.⁴ The court found that since the statute was designed to punish criminals while at the same time ensuring that innocent spouses are not penalized, "prohibiting forfeiture of all homestead property in [Florida] would clearly violate the congressional intent behind the forfeiture statute."⁵ Note, however, that when a judgment is recorded prior to the debtor establishing homestead status, the residence is subject to levy.⁶ This result should follow logically, since any property that is not homestead is subject to creditors claims and a recorded judgment should be respected if in place prior to the time a residence benefits from homestead status.

Questionable and Fraudulent Conveyances

Florida courts have stated in dicta that the homestead exemption should not be used as an instrument of fraud upon creditors.⁷ However, when presented with an opportunity to so hold under circumstances smelling of fraud, the Florida Supreme Court refused to do so. In *Havoco of America, Ltd. v. Hill*, 790 So. 2d 1018 (Fla. 2001), judgment was entered against the debtor, a resident of Tennessee, on December 19, 1990. The enforceability of the judgment was delayed until January 2, 1991. With full knowledge of the judgment, the debtor purchased a Florida home on December 30, 1990, using nonexempt funds that would have been available to the known creditor, intentionally converting them into Florida homestead property. The Florida Supreme Court reasoned that when an equitable lien is sought against homestead real property, there must be proof of some fraudulent or otherwise egregious act by the beneficiary of the homestead protection, and the creditor did not provide such proof.⁸ The Court also noted that the debtor's conversion of funds to avoid a creditor was not one of the three exceptions to the homestead exemption under the Florida Constitution and, therefore, refused to extend equitable principles to permit the creditor to proceed against the debtor's homestead.⁹

The three circumstances set forth in the Florida Constitution under which a forced sale of a homestead may take place, as cited in *Havoco*, are 1) payment of taxes and assessments thereon; 2) obligations contracted for the purchase, improvement or repair thereon; or 3) obligations contracted for house, field or other labor performed on the property.¹⁰ While none of these situations were present in *Havoco*, the court refused to provide equitable relief for the creditors in a situation that appears to have been ideally suited for it.

A potential danger of situation in which there is egregious conduct, however, is the possibility that if the

matter is in bankruptcy court, the bankruptcy court judge many choose to withhold, discharge, or dismiss the bankruptcy altogether, thereby permitting creditors to survive bankruptcy.¹¹ While this potential danger is an example of equitable relief a judge may choose to provide, it is something debtors must be aware of.

Proposed Federal Bankruptcy Legislation

To curb the perceived abuses of the homestead exemption in Florida and other states, Congress has been considering ways to overhaul the nation's bankruptcy laws since 1997. In 2001, separate bankruptcy reform bills were passed by the Sen-

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The following message points were considered carefully before the program commenced and have been delivered:

- 1) The legal profession is widely misunderstood;
- 2) Our job is to make the law work for all Floridians;
- 3) The Florida Bar is the gold standard for protecting the public; and
- 4) Good acts are achieved by lawyers and judges every day.

National coverage has been received on this noteworthy program. I recently spoke at the request of the Philadelphia Bar Association to 150 lawyers and judges in Philadelphia who wanted to learn more about our outstanding program. The Southern Conference of Bar Presidents heard stimulating presentation by our private consultants and, at the conclusion of the presentation, A.P. Carlton, president of the American Bar Association, was enthused by the creativity and effectiveness of the program.

Next Steps: The Dignity in Law program will continue its media outreach, going deeper into our media targets. We will be conducting a joint survey with the Florida Association of Nonprofit Organizations to showcase the vital role that attorneys play in keeping critical nonprofit groups alive. We will begin direct electronic communication to all legislators with a monthly e-mail that will graphically demonstrate positive information about our profession. We will continue to work closely with all voluntary bar associations.

We are exploring several additional avenues to engage consumers including the launching of a

"Shadow-a-Judge" program that offers a behind-the-scenes look at our system of justice through the eyes of a judge; promotions through church/community relations departments to reach underserved populations who do not consume traditional media; and implementation of an educational video/handout materials in jury pool rooms throughout the state.

I am pleased to report the success of the first Dignity in Law All Bar Conference held on January 16, 2003, at the Midyear Meeting of the Florida Bar. This was an outstanding program that was covered by the press statewide and offered a provocative panel discussion by journalists and interaction with leading Florida attorneys on the effect of the Dignity in Law program.

The lawyers and judges of Florida are enthused by this program that draws a line in the sand and states to all Floridians that we, as lawyers and judges, are proud of our profession and are pleased to tell all Floridians of the importance of the work that we do. I urge you to join this effort vigorously by following the progress of the program (www.flabar.org-dignityinlaw) and by telling your partners, associates, clients, and neighbors of your pride in our profession.



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ate and House that, if enacted, would have an enormous impact on the value of a homestead that may escape a bankruptcy. There was much debate and conflict between the House and Senate versions, with one key area of dispute being the unlimited homestead exemption permitted by several states including Florida and Texas. In April 2002, with the threat of a veto from President Bush should Congress attempt to cap state homestead exemptions, the two sides came together and worked through several competing matters.¹²

The House bill, H.R. 333, continued to permit an unlimited homestead exemption. However, it limited the exemption to debtors who had owned their homes for at least two years prior to filing for protection under federal bankruptcy laws. The House bill also included three safeguards to protect against perceived abuses: 1) the exemption will not protect assets that were converted into homestead property if the conversion occurred within seven years prior to filing, and if the court determined that the conversion was done to hinder, delay or defraud creditors; 2) the debtor must have lived in the state of the claimed homestead benefit for 730 days prior to filing for protection (otherwise the law of the prior domicile will generally apply); and 3) if the unlimited exemption is not permitted, then the exemption would be capped at \$100,000.

The Senate Bill, S.420, was much less generous to debtors. It required that they live in the state of the claimed homestead benefit for 730 days prior to filing for protection in order to receive a maximum \$125,000 homestead exemption. If the debtor fails to meet the residency requirement, the homestead exemption of the prior domicile would control. The proposed Senate bill did not permit an unlimited homestead exemption.

Members of the conference committee met on May 22, 2002, but failed to report the bill out of committee because of a deadlock over a matter unrelated to homestead bankruptcy problems.¹³ The compro-

mise bill, if enacted, would have significantly impacted the ability of a person to move to Florida shortly before a bankruptcy filing (or any other state with favorable homestead provisions) to take advantage of its unlimited homestead exemption. The compromise version of H.R. 333 is dead. However, had it been enacted, it would have impacted the exemption by capping the homestead exemption at \$125,000, only if the debtor: 1) could not meet a residency requirement of 40 months in a particular state before filing for bankruptcy; 2) was shown to have committed fraud or other criminal acts, such as violations of state or federal securities regulations, prior to filing for bankruptcy (this provision appears to be aimed at situations such as Enron and WorldCom); or 3) was subject to pending criminal charges. Furthermore, the unlimited homestead exemption would still apply in Florida if the other requirements to qualify for homestead were satisfied. The bankruptcy court would have had the ability to look back 10 years for instances of fraud associated with a homestead exemption claim.¹⁴ Much has been written on whether the compromise bankruptcy bill was fair even though it retains the unlimited homestead exemption.¹⁵ It would appear that any future bankruptcy reform will have as one of its aims the elimination of some of the eve-of-bankruptcy maneuvering that allowed debtors similar to those in the *Havoco* decision to use Florida's homestead as a successful technique to exempt significant assets from the reach of the bankruptcy court.

It should be noted that the compromised bill after being approved by the Senate was defeated in the House by religious conservatives on November 14, 2002. As a result, the House introduced H.R. 5745, an amendment to H.R. 333, which removes §330 from the compromised House bill. Section 330 was the controversial provision which prohibited abortion activists from discharging their debts incurred in connection with protest activities. The Senate did not consider the new

version of the bill and it has been reported that the Senate will no longer act on bankruptcy reform in 2002. In light of the extended negotiations that took place to arrive at the compromise 2002 bankruptcy bill described above, it would appear likely that there will be reform in the future. However, based upon the latest string of criminal indictments of corporate executives, it is possible that legislators may be unwilling to accept a continued unlimited homestead exemption, and advisors must be aware of such a possibility.

Planning

Once a residence satisfies all of the requirements for homestead creditor protection described in this article, other planning issues remain. For example, deciding on the amount of equity to maintain in a residence can be a very difficult decision. From an asset protection viewpoint, a homestead owned free and clear provides the greatest protection to a homeowner because his or her protected equity in the home is equal to its fair market value. However, many financial planners and CPAs maintain that having too much equity in a homestead is wasteful because the owner does not benefit from a mortgage interest deduction and because the funds used to pay off the debt may do better if invested elsewhere. These issues may create conflicts among a client's team of professionals. If asset protection is a significant client objective, we have recommended the benefits of having the smallest affordable mortgage and maintaining the highest equity possible in the homestead. However, on occasion the client's financial planner and/or CPA criticize such planning and advise the client that he or she could benefit from investments that would generate earnings that would exceed the after-tax mortgage interest cost. The authors have been involved in a situation where a client's financial advisor was incensed because a mutual client withdrew funds from his account with the financial planner to pay down a portion of his mortgage, thereby enhancing his

homestead equity.

It is important for the client to make an informed decision on whether to maintain a mortgage on his or her residence if asset protection is an important goal. The tax, financial, and asset protection consequences of each alternative need to be considered. Since the homestead exemption protects the equity in a homestead, the greater the equity in the homestead, the greater the value that will be protected.

While there are many other asset protection techniques effective in Florida, such as annuities, qualified pension plans, IRAs, cash surrender value of life insurance policies, and wage earner accounts, it is the authors' opinion that the best asset protection planning is a diversified approach considering the exemptions of all such options.¹⁶ Furthermore, family limited partnerships, spendthrift trust planning, and domestic and foreign asset protection trusts should be considered to develop a comprehensive asset protection plan. However, the benefits of each such option must be compared with the peace of mind that comes with knowing one's home is protected from creditors. Consequently, for those who are particularly motivated by asset protection planning, the guiding light may be to ensure that their homesteads satisfy all of the homestead requirements described in this article, and that they maintain as much equity as possible in the homestead.

Conclusion

While it may appear that the Florida homestead exemption is unlimited, there are significant restrictions that are not commonly understood by the press and public. A Florida debtor assumes at his or her peril that his or her homestead is exempt in its entirety from a forced sale for the benefit of creditors.

Before a debtor can be confident that the homestead will survive attack by creditors, he or she must be sure that the residence satisfies applicable acreage requirements, be recognized as a homestead, and be titled properly. Even if the home-

stead appears to meet all Florida state law requirements, the U.S. government may, under certain circumstances, pierce the protective armor of homestead protection. In addition, egregious or fraudulent conduct intended to hamstring claims of legitimate creditors could invite a court to do what courts have come close to doing on several prior occasions: carve out an equitable exception to homestead protection. Moreover, if a bankruptcy bill is enacted in the coming months, it will certainly resemble the proposed 2002 bankruptcy bill. Thus, the debtor cannot have engaged in certain types of egregious conduct prior to having filed for bankruptcy, and must satisfy a stringent residency requirement prior to filing for bankruptcy. Finally, a client's legal advisor must be sensitive to the possibility that the client's other advisors may recommend a course of action that is inconsistent with prudent asset protection planning. □

¹*In re McFadyen*, 216 B.R. 1006, 1008 (Bankr. M.D. Fla. 1998).

²*Id.* at 1009 quoting *Thompson v. Adams*, 685 F. Supp. 842, 846 (M.D. Fla. 1988) quoting *U.S. v. Estes*, 450 F.2d 62, 65 (5th Cir. 1971).

³*United States v. One Single Family Residence Located at 212 Airport Rd. South, et.al.*, 771 F. Supp. 1214, 1215 (S.D. Fla. 1991), quoting 894 F.2d 1517 (11th Cir. 1990).

⁴*United States v. One Single Family Residence Without Building, et.al.*, 894 F.2d 1517 (11th Cir. 1990).

⁵*Id.* at 1216.

⁶*Kirkland v. Kirland*, 253 So. 2d 728, 730 (Fla. 3d D.C.A. 1971); *Aetna Ins. Co. v. LaGasse*, 223 So. 2d 727, 728 (Fla. 1969); *Carrington*, 214 F. Supp. 2d 1348 citing *Bessemer v. Gersten*, 381 So. 2d 1344, 1347 n.1 (Fla. 1980).

⁷*Simpson v. Simpson*, 123 So. 2d 289, 294 (Fla. 2d D.C.A. 1960); *Fraser v. Branch*, 362 So. 2d 317, 319 (Fla. 2d D.C.A. 1978) ("Great care should be taken to prevent homestead laws from becoming instruments of fraud, an imposition on creditors, or a means to escape honest debts"); *Englander*, 95 F.3d at 1031 ("The homestead exemption law is intended to be a shield, not a sword, and should not be applied as to make it an instrument of fraud or as an imposition upon creditors").

⁸*Havoco*, 790 So. 2d at 1027.

⁹*Id.* at 1028.

¹⁰*Id.* at 1022.

¹¹*Havoco*, 197 F.3d 1135, 1143 n.12. ("Adding to the confusion in this area is

the conclusion of some courts that, although a debtor's fraudulent conversion of non-exempt assets into a homestead does not provide a basis for denying him the homestead exemption, the debtor's fraudulent transfer may serve as the predicate for denying the discharge. See, e.g. *Marine Midland Bank, N.A. v. Mellon*, 160 B.R. 860 (Bankr. M.D. Fla. 1993) (denying discharge under 11 U.S.C. §727(a)(2)(A) when the debtor who clearly by law is entitled to convert nonexempt assets to exempt assets did so in this case with a fraudulent intent"); *In re Hendricks*, 237 B.R. 821, 826 (Bankr. M.D. Fla. 1999); *In re Young*, 235 B.R. 666, 671 (Bankr. M.D. Fla. 1999))."

¹²BANKR. L. DAILY (BNA) (May 31, 2002).

¹³*Id.*; Greg Hitt and Christine Whelan, *Bankruptcy-Reform Bill Displays Still-Formidable Corporate Clout*, THE WALL STREET JOURNAL ONLINE, July 29, 2002.

¹⁴BANKR. L. DAILY (BNA) (April 24, 2002).

¹⁵Dawn Kopecki, *Deal Paves Way for New Bankruptcy Law; House Vote Seen Friday*, THE WALL STREET JOURNAL ONLINE, July 26, 2002; Dawn Kopecki, *US House Expected to Adopt Harsh New Bankruptcy Laws*, THE WALL STREET JOURNAL ONLINE, July 26, 2002; Kathleen Day, *Hill Set to Toughen Bankruptcy Law*, THE WASHINGTON POST, July 26, 2002; *Bankruptcy reform bill moves forward*, USA TODAY, July 26, 2002; Rob Wells, *Passage of Bankruptcy Bill Now Trickier For US Congress*, THE WALL STREET JOURNAL ONLINE, July 29, 2002; *US House Adjourns Without Acting on Bankruptcy Bill*, THE WALL STREET JOURNAL ONLINE, July 29, 2002; and Philip Shenon, *Vote on Bankruptcy Bill is Stalled by Abortion Provision*, THE NEW YORK TIMES, July 30, 2002.

¹⁶See, FLA. STAT. ANN. §222.13 222.25 (2002).

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