

The Benefits of a Series LLC



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THE LIMITED LIABILITY COMPANY (LLC) has become the business entity of choice in the United States for the holding of real estate as well as for many other business and investment ventures. The LLC allows business owners to achieve limited liability for debts of the business while being taxed on a favorable pass-through basis.

A number of states—including Delaware, Illinois, Iowa, Oklahoma, Nevada, Tennessee, and Utah—have now enacted provisions allowing for the creation of what is referred to as a “Series Limited Liability Company” (SLLC). A SLLC can designate separate series (or divisions) within the entity into which operations, assets and ownership interests can be segregated.

A Series LLC can be structured to allow each series to stand alone but under one umbrella entity. This allows each series to have its own business or investment purpose, classes of ownership interest, managers, and liability limitations without the costs of forming and operating multiple LLCs or subsidiaries.

Series LLCs promise to offer numerous benefits for those operating multiple businesses including: avoiding the cost of forming multiple LLCs or subsidiaries; the possibility of reducing administrative expenses and state filing fees, such as franchise tax fees required to be paid in some states for LLCs; the ability to add new series within the LLC without additional filings with the Secretary of State; the ability to dissolve a series within the LLC without affecting the other series within the LLC; the ability to make tax-free transfers within the LLC; and the ability to segregate liabilities within a series.

For example, a Series LLC can be structured to hold multiple parcels or projects of real property insulated from each other in a separate series, but under a single umbrella entity. Other examples where it promises to offer tremendous advantages in planning are for such



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businesses as hedge funds, venture capital funds, chain retail establishments or multiple franchise operations, oil and gas deals, etc. The ability to hold each property or operation in a separate series may save the owner thousands of dollars in startup costs as well as in ongoing administrative and state tax costs.

Until recently, there has been little formal guidance on the tax treatment of the Series LLC. A recent IRS and Massachusetts state ruling hold promise that the anticipated benefits can be accomplished.

The IRS recently issued some guidance in the form of a letter ruling regarding the federal tax treatment of a Delaware formed Series LLC. It held that each series of the LLC in question was a separate entity for federal tax purposes. Further, as a separate entity, the IRS said that each series could make its own entity election. For example, one series could elect to be taxed as a disregarded entity while another elected to be taxed as a partnership. The available elections depended on the characteristics of the series. In other words, a single member series could elect to be treated as a corporation or disregarded entity, while a multiple member series had the option of electing to be a partnership or a corporation. Letter rulings, of course, are binding only on the taxpayer requesting the ruling. Nevertheless, the IRS analysis in this ruling indicates its current position and thinking in regard to Series LLCs.

In a Massachusetts ruling for state income tax purposes, the Massachusetts Department of Revenue ruled that each LLC series in question (in this case, also a Delaware LLC) should be classified as a separate entity for Massachusetts income tax purposes. Although not conclusive, this is another step in the right direction indicat-

continued on page 64

Is Your 401(k) Plan Complying with Timely Remittance Requirements?

continued from page 58



DOL's Web site, www.dol.gov, which allows companies to self-correct a delinquency. This action still requires the company to make additional contributions to the plan participants for lost earnings, but it avoids penalties or excise taxes normally assessed by the DOL.

Companies establish 401(k) plans to assist employees with saving for retirement and to show their appreciation by making matching contributions. However, if the company is not remitting the contributions on a timely basis, then it is not appropriately honoring the spirit of the plan and may be opening itself up to scrutiny and potential penalties by the DOL and the IRS.

Accordingly, the management of companies with 401(k) plans need to regularly evaluate employee deferral contributions remittance policies to ensure compliance with the DOL requirements. Of course, there are other options available to companies seeking to mitigate this issue. Using automated payroll companies to manage the remittance process or implementing a formal internal control procedure are among other measures. ■

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The Benefits of a Series LLC

continued from page 60



ing that in Massachusetts a Series LLC should be able to realize the hoped-for cost savings and asset protection benefits, while still allowing the flexibility to make individual entity elections.

On the other hand, the California Franchise Tax Board recently indicated that California will view Series LLCs as being multiple (separate) LLCs that must pay multiple California LLC annual taxes and fees. This means that Series LLCs in California won't see all the hoped-for cost savings (i.e., their filing fees will not be reduced).

Although these rulings don't answer all the questions surrounding Series LLCs, they are definitely a step in the right direction.

A number of important questions remain unanswered about the practicalities of the Series LLC. For example, will a court be willing to allow creditors to "pierce the veil" between series, and, if so, under what conditions? More states—including New Jersey—need to issue guidance on how they will embrace and interpret the Series LLC under their tax and other laws. These are just some of the issues that will need to be resolved in the coming years.

As time passes, I expect to see more Series LLCs, especially if more states adopt favorable interpretations and other unanswered questions become clear—not unlike the trend toward using LLCs that took off in the 1990s, more than a decade after the first modern LLC concept was adopted by the Wyoming legislature in 1977. ■

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