

JOHN CUNNINGHAM'S LLC NEWSLETTER FOR TAX AND FINANCIAL PROFESSIONALS

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DO YOUR CLIENTS' LLCs NEED FIXING?

Part I – INTRODUCTION AND SUMMARY

Introduction.

There are now about 23,000 New Hampshire LLCs (as compared with about 25,000 New Hampshire corporations). Half of these LLCs have only a single member. Most of the rest have two members. A small number have three or more members.

Based on my involvement over the past 10 years with literally hundreds of LLCs that have been formed by their own members or by lawyers who lack significant LLC expertise, I believe that as many as half of these 23,000 LLCs – in other words, a good 11,500 of them - have been formed incorrectly and have potentially serious legal or tax flaws. These 11,500 LLCs need repair. If any of them are owned by clients of yours, you can do these clients an important service by making sure their LLCs get these repairs.

In this issue of my newsletter, I'll list the 13 principal errors that, in my experience, people who lack LLC tax and legal expertise are likely to make in forming LLCs. In the following two issues, I'll discuss these errors in greater detail and I'll explain how to fix them.

Forming LLCs – the Top 13 Errors

You're not an accountant or a lawyer, but you've decided to form your own LLC. In doing so, what are the main errors you're likely to have made?

A. SINGLE-MEMBER LLCs (ERRORS 1-8)

ERROR NO. 1. Single- or multi-member LLC – failure to address veil-piercing risk and asset protection problems. You've formed a single- or multi-member LLC, but you've failed to take basic measures to protect your LLC liability shield and to maximize LLC statutory asset protection. (Needless to say, people who have formed a multi-member LLC can make this same error.)

ERROR NO. 2. Too few entities. You've formed a single-member LLC, but to maximize business asset protection, you should have formed two of them. (Needless to say, people who have formed a multi-member LLC can make this same error.)

- ERROR NO. 3. Single-member LLC – too few members for business effectiveness. You formed a single-member LLC, but, in order to maximize business effectiveness, it should have been a multi-member LLC.
- ERROR NO. 4. Single-member LLC – too few members to provide business asset protection. You formed a single-member LLC, but, in order to obtain business asset protection, it should have been a multi-member LLC.
- ERROR NO. 5. Single-member LLC – too few members to avoid Social Security taxes. You formed a single-member LLC, but, in order to minimize Social Security taxes, it should have been a multi-member LLC.
- ERROR NO. 6. Single-member LLC – failure to make S election. You formed a single-member LLC, but when you did so, you should have made an S election to minimize Social Security taxes.
- ERROR NO. 7. Single-member LLC – failure to consider Interest and Dividends Tax problems. You formed a single-member LLC, but in order to avoid the New Hampshire Interest and Dividends Tax, you should have formed a two-member LLC.
- ERROR NO. 8. Single-member LLC – failure to adopt LLC agreement. You formed a single-member LLC, but your LLC has no written LLC agreement.

B. MULTI-MEMBER LLCs (ERRORS 9-13)

- ERROR NO. 9. Multi-member LLC – partnership – failure to address federal income tax problems. You formed a multi-member LLC taxable as a partnership, but you didn't structure it to avoid partnership federal income tax problems.
- ERROR NO. 10. Multi-member LLC – partnership – failure to address Social Security tax problems. You formed a multi-member LLC taxable as a partnership, but you didn't structure it to minimize Social Security taxes.
- ERROR NO. 11. Multi-member LLC – failure to address I&D Tax problems. You formed a multi-member LLC, but you didn't structure it to protect the members from the New Hampshire Interest and Dividends Tax.
- ERROR NO. 12. Multi-member LLC – failure to make S election. You formed a multi-member LLC, but, in order to minimize Social Security taxes, you should have made an S election for it.
- ERROR NO. 13. Multi-member LLC – failure to adopt LLC agreement. You formed a multi-member LLC, but you and your co-members didn't negotiate and sign an LLC agreement.