

**JOHN CUNNINGHAM'S LLC NEWSLETTER  
FOR TAX AND LEGAL PROFESSIONALS**

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**CHECKLIST FOR ACCOUNTANTS HELPING THEIR  
CLIENTS TO FORM LLCs**

EXECUTIVE SUMMARY. There are 18 professional tasks that normally must be performed in assisting clients to form LLCs and other legal entities. These tasks are identified in the checklist below. As the checklist makes clear, nine of the tasks require a substantial knowledge of federal and state taxation of business entities and their owners. Many accountants possess this knowledge, but few lawyers do. Most of the rest of the 18 tasks require a knowledge of statutory business organization law and generally may be handled only by professionals licensed to practice law.

However, all legal and tax professionals who assist clients in forming LLCs should be familiar with the checklist and should ensure that specific tasks identified in it that are beyond their own professional expertise are handled for their clients by other professionals who possess this expertise.

THE CHECKLIST

Note. The term "tax" as used below is intended to refer simultaneously to federal income tax, Social Security Tax and state tax.

<b>CHECK WHEN TASK IS ACCOMPLISHED</b>	<b>TASKS (IN THE ORDER IN WHICH THEY SHOULD NORMALLY BE HANDLED)</b>	<b>AREA OF EXPERTISE REQUIRED</b>	<b>EXPLANATORY COMMENTS (WHERE NEEDED)</b>
<input type="checkbox"/>	1. IDENTIFY AND HANDLE ALL RELEVANT ETHICAL ISSUES.	PROFESSIONAL ETHICS	The principal relevant issues concern (i) professional competence in handling the tasks listed in this table; and (ii) (if two or more clients are involved) conflicts of interest
<input type="checkbox"/>	2. OBTAIN ALL RELEVANT BACKGROUND FACTS.	BUSINESS ORGANIZATION LAW AND TAX	

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<input type="checkbox"/>	3. DETERMINE OPTIMAL NUMBER OF ENTITIES.	BUSINESS ORGANIZATION LAW	Many start-up businesses should be structured to include a holding company (to hold valuable business assets) and an operating company (to which the holding company will lease, license or lend these assets).
<input type="checkbox"/>	4. DETERMINE OPTIMAL NUMBER OF OWNERS FOR EACH ENTITY.	BUSINESS ORGANIZATION LAW	Under the case of <i>In re Albright</i> , holding companies should have at least two owners in order to ensure charging order protections.
<input type="checkbox"/>	5. DETERMINE OPTIMAL FEDERAL INCOME TAX REGIMEN FOR EACH ENTITY FOR FEDERAL INCOME TAX PURPOSES.	FEDERAL INCOME TAXATION	The choice will generally be among sole proprietorship taxation and taxation under Subchapters C, K and S.
<input type="checkbox"/>	6. DETERMINE OPTIMAL FEDERAL INCOME TAX REGIMEN FOR EACH ENTITY FOR SOCIAL SECURITY TAX PURPOSES.	SOCIAL SECURITY TAXATION	Use of Subchapter S can be a powerful means to avoid Social Security Taxes. The use of Prop. Reg. § 1.1402(a)-2 may be necessary to protect from Social Security Tax individuals who are members of LLCs taxable as partnerships.
<input type="checkbox"/>	7. DETERMINE OPTIMAL FEDERAL INCOME TAX REGIMEN FOR EACH ENTITY FOR STATE TAX PURPOSES.	STATE TAXATION	In most states, entities that receive pass-through taxation for federal income tax purposes will also receive state pass-through taxation

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<input type="checkbox"/>	8. IF NECESSARY, RECONCILE TASKS 5-7.	FEDERAL AND STATE TAX	The federal income tax regimen that is best for federal income tax purposes may sometimes not be the best for Social Security Tax avoidance purposes or for state tax purposes.
<input type="checkbox"/>	9. DETERMINE OPTIMAL STATE-LAW BUSINESS ORGANIZATION FORM FOR EACH ENTITY FOR NON-TAX PURPOSES.	BUSINESS ORGANIZATION LAW	Nontax choice of entity analyses can generally be resolved by considering three factors—limited liability; charging order protections; and management structure.
<input type="checkbox"/>	10. DETERMINE OPTIMAL STATE-LAW BUSINESS ORGANIZATION FORM FOR EACH ENTITY FOR STATE TAX PURPOSES.	STATE TAXATION	In some states, some types of business entities may receive better tax treatment than others—e.g., Texas, where the Franchise Tax applies to corporations and LLCs but not to general and limited partnerships.
<input type="checkbox"/>	11. IF NECESSARY, RECONCILE TASKS 9 AND 10.	BUSINESS ORGANIZATION LAW AND TAX	
<input type="checkbox"/>	12. DO A CHECK-THE-BOX ANALYSIS FOR EACH ENTITY AND DO ANY NECESSARY RECONCILIATION OF TASKS 5-11	FEDERAL INCOME TAXATION	The Check-the-Box Regulations determine what type of federal income taxation is available for each type of state-law business entity.
<input type="checkbox"/>	13. DETERMINE OPTIMAL BUSINESS ORGANIZATION LAW STATUTE UNDER WHICH TO FORM EACH ENTITY.	BUSINESS ORGANIZATION LAW	For high-stakes entities, Delaware business organization law statutes are often preferable.

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<input type="checkbox"/>	14. DETERMINE OPTIMAL MANAGEMENT STRUCTURE FOR EACH ENTITY.	BUSINESS ORGANIZATION LAW	The main types of LLC management structures are the sole proprietorship structure, the general and limited partnership structures and the corporate structure. The decision as to which management is best for a given entity can be complex.
<input type="checkbox"/>	15. ASSUMING THAT ONE OR MORE ENTITIES SHOULD BE LLCs, DETERMINE THE LLC TYPE THAT BEST DESCRIBES EACH RELEVANT LLC AND, ON THAT BASIS, DETERMINE THE BEST MODEL OPERATING AGREEMENT FOR USE IN FORMING EACH LLC.	BUSINESS ORGANIZATION LAW AND FEDERAL INCOME AND SOCIAL SECURITY TAX	On the basis of the number of their members, their management structures and their tax structures, there are 14 main types of LLCs and 37 main types of model operating agreements.
<input type="checkbox"/>	16. IN PLANNING, NEGOTIATING AND DRAFTING THE TERMS OF THE INTER-OWNER AGREEMENT FOR EACH ENTITY IN QUESTION, ADDRESS ALL RELEVANT BUSINESS ORGANIZATION LAW ISSUES.	BUSINESS ORGANIZATION LAW	There are five main types of LLC business organization law issues—basic factual and structural issues; financial issues; management issues; fiduciary issues; and “miscellaneous” issues (including issues relating to dissociation events, dissolutions and “boiler plate” provisions).
<input type="checkbox"/>	17. IN PLANNING, NEGOTIATING AND DRAFTING THE TERMS OF THE INTER-OWNER AGREEMENT FOR EACH ENTITY IN QUESTION, ADDRESS ALL RELEVANT FEDERAL AND STATE TAX ISSUES.	FEDERAL AND STATE TAXATION	The federal income tax issues that should be addressed in owner agreements will vary greatly depending on the federal income tax regimen to which the entity in question is subject.

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<input type="checkbox"/>	18. IN PLANNING, NEGOTIATING AND DRAFTING THE TERMS OF THE INTER-OWNER AGREEMENT FOR EACH ENTITY IN QUESTION, ADDRESS ALL RELEVANT "MISCELLANEOUS" LEGAL ISSUES.	GENERAL BUSINESS LAW	Miscellaneous issues are issues that are neither business organization law issues nor tax issues. Examples include securities law issues and fraudulent transfer issues.