

Hurry and Use the Restricted LLC/LP Statutes Before the IRC Section 2704 Regulations are Finalized!

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Estate planners often use family limited liability companies and family limited partnerships to facilitate gifting and installment sales of minority interests or non-voting interests to family members or irrevocable trusts for the benefit of family members.

Under Code Section 2704(b) and Treasury Regulations §25.2704-2(a), if an interest in an entity is transferred to or for the benefit of a member of the transferor's family, any applicable restriction is disregarded in valuing the transferred interest. Treasury Regulations §25.2704-2(b) defines an applicable restriction as a limitation on the ability to liquidate the entity (in whole or in part) that is more restrictive than the limitations that would apply under the state law generally applicable to the entity in the absence of the restriction.

Until 2009, all states have been limited to some form of the Uniform Laws. A number of states, including Nevada, have had favorable default restrictions that allow for slightly higher valuation discounts than the discounts that can be obtained using other states' laws.

But Nevada separated its valuation discount opportunities significantly in comparison to all other states. Specifically, Nevada Senate Bill 350 was signed into law by the Governor on May 29, 2009. One of the provisions of the new law, effective October 1, 2009, allows the creation of a Restricted LLC or a Restricted LP.

The difference between a Restricted LLC and Restricted LP versus a standard LLC and LP is that the Restricted LLC and LP have a default statute locking in the entity's underlying assets for a ten-year period. This creates a new significantly higher ceiling on valuation discounts that is not available in any other



state since the current laws look at the state default provisions on liquidation.

The Proposed Treasury Regulations, on the other hand, would disqualify these additional provisions from being used by the appraiser in valuing the transferred interests. Thus, there should be a mad rush to form Nevada Restricted LLCs and LPs and make transfers as soon as possible and before the new Final Treasury Regulations are issued.

NEW STATUTES – RESTRICTED LLC

The primary statutory provisions creating the Restricted LLC laws read as follows:

1. "Restricted limited-liability company" means a limited-liability company organized and existing under this chapter that elects to include the optional provisions permitted by NRS 86.161.
2. If a limited-liability company has elected in its articles of organization to be a restricted limited-liability company pursuant to NRS 86.161, subject to the provisions of NRS

86.343, and unless otherwise provided in the articles of organization, the company shall not make any distributions to its members with respect to their member's interests until 10 years after:

(a) The date of formation of the restricted limited-liability company as long as the original articles of organization elected to be treated as a restricted limited-liability company and as long as the company has remained a restricted limited-liability company since the date of formation; or

(b) The effective date of the amendment to the articles of organization in which the company elected to be treated as a restricted limited-liability company and as long as the company has remained a restricted limited-liability company since the effective date of the amendment.

3. The provisions of this section apply as the default provisions of a restricted limited-liability company to the extent the provisions of this section are inconsistent with or add to the other provisions of this chapter and to the extent not otherwise modified in the articles of organization of the restricted limited liability company.

NEW STATUTES – RESTRICTED LP

The primary statutory provisions creating the Restricted LP laws read as follows:

1. "Restricted limited partnership" means a limited partnership organized and existing under this chapter that elects to include the optional provisions permitted by NRS 87A.235.

2. If the limited partnership has elected in its certificate of limited partnership to be a restricted limited partnership pursuant to NRS 87A.235, subject to the provisions of NRS 87A.425, and unless otherwise provided in the certificate of limited partnership, the limited partnership shall not make any distributions to its partners until 10 years after:

(a) The date of formation of the restricted limited partnership as long as the original certificate of limited partnership elected to be treated as a restricted limited partnership and as long as the limited partnership has remained a restricted limited partnership since the date of formation; or

(b) The effective date of the amendment to the certificate of limited partnership in which the limited partnership elected to be treated as a restricted limited

partnership and as long as the limited partnership has remained a restricted limited partnership since the effective date of the amendment.

3. The provisions of this section apply as the default provisions of a restricted limited partnership to the extent the provisions of this section are inconsistent with or add to the other provisions of this chapter and to the extent not otherwise modified in the certificate of limited partnership of the restricted limited partnership.

4. If the limited partnership has elected in its certificate of limited partnership to be a restricted limited partnership pursuant to NRS 88.350, subject to the provisions of NRS 88.520, and unless otherwise provided in the certificate of limited partnership, the limited partnership shall not make any distributions to its partners with respect to their partnership interests until 10 years after:

(a) The date of formation of the restricted limited partnership as long as the original certificate of limited partnership elected to be treated as a restricted limited partnership and as long as the limited partnership has remained a restricted limited partnership since the date of formation; or

(b) The effective date of the amendment to the certificate of limited partnership in which the limited partnership elected to be treated as a restricted limited partnership and as long as the limited partnership has remained a restricted limited partnership since the effective date of the amendment.

5. The provisions of this section apply as the default provisions of a restricted limited partnership to the extent the provisions of this section are inconsistent with or add to the other provisions of this chapter and to the extent not otherwise modified in the certificate of limited partnership of the restricted limited partnership.

FLEXIBILITY OF THE RESTRICTED LLC/LP STATUTES

Remember that the Nevada Restricted LLC and LP statutes only create a new higher ceiling on valuation discounts that no other state allows. This doesn't mean that the drafting attorney must lock the underlying assets in for ten years. Maybe five years is more appropriate. Maybe three years.

In certain cases, the operating agreement or partnership agreement might be drafted to lock the underlying assets in for ten years but with the discretionary right to distribute up to ten percent per year. Maybe five percent. Maybe enough

to pay any income tax liability. The draftsman will make this determination when creating the plan.

CONCLUSION

The possibilities are endless. The creative draftsman will design the Restricted LLC or LP around the contemplated transaction. For example, if the transaction requires annual distributions from the business entity in order to meet a payment obligation, such as an annuity payment required for a Grantor Retained Annuity Trust, the operating agreement or partnership agreement can include language permitting an amount up to a certain specified amount to be distributed from the entity each year.

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