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MAINTENANCE & TAX REPORTING INFORMATION FOR YOUR LIMITED LIABILITY COMPANY (LLC)

Your Limited Liability Company is a distinct legal business entity with its own tax ID number. Note, however, that if *your Limited Partnership is the sole member of your LLC, then it will use the tax id number of your Partnership for tax filing purposes*. Your LLC will also have its own assets and a business purpose (as stated in your documents). As such, it generates income and has business expenses that can reduce the amount of taxable income passing through to the members. Therefore, there are things that must be done in order to treat it as a distinct business entity, and assist your accountant in preparing your annual return.

Purpose

A Limited Liability Company “LLC” is designed to hold risky assets or a business venture that may have liability exposure. Risky assets include any office buildings, investment real estate, rental properties, and any recreational vehicles such as boats or planes. The LLC is designed to compartmentalize that risk so that it would be hard for someone to sue you and attach the assets held in that entity. Additionally, if someone were to try and sue your LLC, they would normally not be able to attach your personal assets. The Limited Liability Company does exactly what its name suggests: it limits the liability to only that entity, rather than to its members.

Registered Agent

Your LLC will normally have been filed by our office in the state where the real estate to be owned by your LLC is located or where your activity will primarily occur. Normally, you are the registered agent for your LLC. The registered agent is the individual designated to receive any formal notices or service of process if the LLC is sued. The registered agent also receives all correspondence from the State Corporation Commission or Secretary of State concerning the LLC. The Registered Agent must have a physical mailing address in the state where the LLC is filed (no PO Boxes).

Wyoming and Delaware LLCs

Wyoming and Delaware LLCs may be used for privacy reasons. If established, the Wyoming LLC or Delaware LLC will serve as the general partner of the Limited Partnership in place of the individual.

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Members

In most cases, the original and sole member of the LLC will be your Limited Partnership. Owners of an LLC are referred to as "Members." The Members will act either by a formal meeting or written consent in place of a meeting. An annual meeting should be held each year, and can be done in conjunction with your meeting for your LP. Other meetings may be held from time to time, and should be held whenever any changes or decisions are made regarding the LLC, or its assets. A written consent in place of any such meeting may be proper.

Management

Under the Agreement, the Members may elect a designated member or members to manage the Company and who will be responsible for most decisions that will be made with respect to the operation of the Company. If your Limited Partnership is the only member of your LLC, then you, as the General Partner of the Partnership will be directly responsible for managing the LLC. The admission of new members and certain extraordinary actions require the approval of the Members.

Minutes

You should keep minutes of any member meetings, and as often as necessary to keep a proper record of the activity of the LLC, such as the transfer of assets in or out of the LLC, a change in the members, or a change of statutory agent. A blank form for meeting minutes is provided at the back of your binder. Remember that the more formalities you take, such as holding meetings, keeping minutes, and keeping accurate accounting records, the more effective your LLC will be to protect your assets if challenged.

Dissolution and Liquidation

The LLC will be dissolved and liquidated if the Limited Partnership, or the members, decide to do so. LLC's are dissolved by filing the appropriate form and paying a small fee to your Secretary of State's office. Once the LLC is dissolved, it may be liquidated by selling the assets to satisfy its liabilities, and distributing the net proceeds to the Members.

Amendment of Operating Agreement

The Agreement may be amended by the consent of all the Members. It is important to document all changes to the members, or membership interests, and keep these records with your LLC binder. Certain amendments, such as a change to the name of your LLC, the statutory agent, or in some cases, a change to the members, must be filed with your Secretary of State. This is done by filing a form, and paying a small fee. Most Secretary of State offices have a corporations or business division that makes its forms available on-line. Contact our office if you have questions, or would like assistance.

Non-Tax Benefits of Companies

In addition to some potential tax savings that may be achieved by using an LLC to hold your assets, the LLC will benefit you and your descendants in a number of other important ways. By

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transferring real property to the LLC, you will consolidate the administration of the property, and thus minimize the expense associated with maintaining the property. Furthermore, as you or the other Members wish to transfer partial interests in the LLC to your respective beneficiaries, you will be able to do so without the expense and trouble of executing multiple deeds for real estate or other documents relating to the transfer of securities or other personal property. Finally, because the property will be owned by the LLC rather than you, your heirs will avoid some of the expense and burdens associated with probate, and, to the extent that you give away interests in the LLC, you will avoid probate altogether with respect to the gifted property.

Obtaining a Federal Tax ID Number

You should obtain a Federal Tax Identification Number (also called EIN or Employment Identification Number) for your LLC. Like a social security number for an individual, this number will identify the LLC for tax purposes. The application for this number is called an SS-4 and one is included with your documents. Please follow the instructions for filing these forms with the Internal Revenue Service. **If the LLC has more than one member**, the LLC will be a separate taxable entity for federal tax purposes, and will need to file a return. **If you have an Asset Management Limited Partnership or Family Limited Partnership that is the SOLE member of the LLC**, you still need to apply for an EIN for the LLC, but the LLC will NOT have to complete an independent tax return. As a single member LLC, it will be considered a *disregarded entity* for tax purposes, and all accounting for the LLC will be completed on the FLP return Form 1065.

Establish a Checking Account

We recommend that you open a checking account in the name of the LLC. If possible, open the account within twenty days of signing the agreement, and deposit at least \$100, or other amount listed in section 2.1 of the Agreement. This checking account will provide the means by which the LLC will pay its ongoing expenses (such as property taxes, legal fees, and other administrative expenses). These fees should be paid out of the LLC account so that they may be properly accounted for on the tax return that will be prepared for the LLC. The legal fees attributable to the organization of the LLC may be deducted against the LLC income over the first five years of the LLC's existence. This is true even if the LLC has only the LP as the sole member.

Hold an Annual Meeting

We generally conduct an annual meeting each year for your Limited Partnership, which would include a discussion of assets held therein, i.e. your LLC assets. This is conducted with you via phone and then we email you completed annual meeting minutes for your file. However, it is best to hold a separate annual meeting for your LLC, especially if there are multiple members that vary from those holding an interest in your Limited Partnership.

Keep Minutes for your Limited Liability Company

Minutes are required for most businesses and you should keep them for your LLC. They consist of a review of your annual and any other business meetings, as well as a listing of the issues discussed regarding the business activities, and a record of the actions that the partners choose to

take. For example, if you are considering diversifying your investments into rental real estate, and discussed setting up a purchasing such real estate, you would note that in your minutes. Although we do send minutes that we take during our annual meetings with you regarding your Partnership, you should also keep minutes for any other meetings or management decisions you are making specifically with regard to the LLC. A form for your LLC Minutes is provided at back of your portfolio for your reference.

Appraisals

You may wish to give away interests in the LLC. For gift and estate tax purposes, it will be important to determine the value of the interests in the LLC that you transfer to your beneficiaries. To do this, you will need to obtain a set of appraisals for the LLC.

The first appraisal should be prepared by a qualified real estate appraiser and it should indicate the value of the real estate owned by the LLC for gift and estate tax purposes. Since your Limited Partnership will often be the only member, you may wish to give limited partnership interests instead of LLC interests. If you are considering gifting interests, please contact our office.

If the LLC owns assets other than real estate and you decide to give away interests in the LLC, rather than interests in the property itself, then you will also need to obtain an appraisal of the LLC. This appraisal should be prepared by a qualified business appraiser. The business appraiser will review the operating agreement for the LLC. Because each member's right to withdraw assets from the LLC is very limited, the value of a transferred interest in the LLC should be lower than the value of the corresponding interest in the real estate that is owned by the LLC. We will be happy to recommend a qualified business appraiser to you if you would like us to.

These formal appraisals will be required in order to establish the value of the transfers for federal tax purposes. Although these appraisals may appear to be unnecessary expenses, we are finding that the Internal Revenue Service is increasingly scrutinizing valuations for gift and estate tax purposes. Therefore, we believe these appraisals are essential if you are going to transfer interests in the LLC.

Maintain a record of deductible business expenses for such things as: Legal and accounting fees; Broker's fees; Books, subscriptions, newsletters; Business supplies; Bank charges; Misc. business travel; Office or business equipment; Printing, postage, etc.; Travel and accommodation; Appraisal fees; Seminars or workshops that enhance the skills of Managing Member and expenses for meetings that may benefit LLC management and further the business purpose of the LLC; as well as any other expenses that your accountant or tax preparer deems appropriate.

How to Amend an Existing Operating Agreement and Articles of Organization

Operating Agreement defines each member(s) rights, powers and entitlements. When LLC members wish to amend an existing operating agreement they create a document titled "amendment" which leaves the prior agreement in force, however, amends specific sections

of the original operating agreement. Amendments are best for small changes—please follow the steps below:

- 1) Make sure that the original Operating Agreement states it can be amended at any time by the company members.
- 2) Then create an Amendment to the LLC Operating Agreement that states the changes. Make sure that the amendment indicated the approval or affirmative vote of all members that would be required to amend the articles of organization. If you need a sample amendment form—please contact our office at 1-800-231-7112.

Articles of Organization act as a charter to establish the existence of your LLC with the state and set forth certain basic information about the new business. Filed as a single document with the Secretary of State's office (or similar state agency that handles business registration). Once filed and approved by the state, the articles of organization legally create the LLC as a registered business entity within the state. The contents of the document are a matter of public record on file.

What is Included in the Articles of Organization? No matter the type or size of your new business, most states require that an LLC's articles of organization include, at a minimum, the following information:

- Your new LLC's name and address (principal place of business)
- The nature of the LLC's business (usually stated in broad language such as "to engage in any lawful activity," in order to avoid limiting the LLC's business prospects)
- Name and address of your LLC's registered agent, who will be authorized to physically accept delivery of certain legal documents (including lawsuits) on behalf of your LLC.
- Name(s) of manager(s) and members of the LLC, if known at the time of filing.

To make changes to the Articles of Organization you will need to check with the appropriate department in the state where the LLC was filed to get the amendment form and filing instructions that is required in that state.

TAX REPORTING INFORMATION FOR YOUR LIMITED LIABILITY COMPANY

In cases where a Limited Partnership is the single member of an LLC, the LLC is treated as a “disregarded entity” and is not required to file. Single member entities include individuals or married couples filing jointly. Instead, all accounting is reported on the Limited Partnership's Form 1065. If the LLC member is an individual, the LLC's income and expenses go on a Schedule C of the individual's Form 1040.

If it is not a single-member LLC, the LLC can be treated for filing purposes, either as a corporation or as a partnership (which is recommended). When treated as a partnership, the LLC would file a Form 1065 with a Schedule K-1 going to each of the partners, indicating their respective share of any taxable income.

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Tax Treatment of an LLC

In addition to limiting personal liability and protecting assets, your LLC can also provide numerous business and tax-saving benefits.

1. An LLC can have exactly the same tax treatment as an S-Corporation. Whether to form a company as an LLC or a corporation is not an either/or proposition. A company can be both—in effect, enjoying the liability protection offered by an LLC and the tax benefits of corporate status. **An LLC is not a tax structure.** It is simply a form of business entity that provides (1) personal liability protection for the manager and members of the company, (2) a simple management structure, (3) minimal reporting requirements and fees, and (4) a format for utilizing the numerous tax benefits accorded a business.
2. Whether an LLC is owned by one person or a group of people, it can elect how it wants to be taxed, i.e., as a sole proprietorship, partnership, sub-chapter C corporation or sub-chapter S corporation, depending on the specific tax issues involved. For example, an LLC that receives exempt income, such as royalties, rental income or investment income is not subject to self-employment (SE) tax. In this case, it makes sense to have the company taxed as a “sole proprietorship” and have the income pass through to the individual owner’s 1040 return and not have to file a separate tax return. This is done by reporting the LLC income, deductions and credits on a 1065 return, with each partner receiving a K-1 for reporting on his or her personal return. However, independent contractors such as plumbers, realtors, and others may determine to operate as an LLC and elect sub-S corporation tax status, which could result in significant social security tax savings—for Example: if you choose to elect S-Corp tax status you must file an IRS form 2553, etc. within prescribed time limits. **As with any tax matter, you should consult with your tax advisor as to how your LLC should elect to be treated for tax purposes.**
3. Converting a corporation to an LLC: A corporation can convert to LLC status in one of two ways. First, if you have already formed a corporation *and* a limited liability company, you can merge the corporation into the LLC. If you want to convert your corporation to a new LLC and maintain the same name, however, you must first dissolve the corporation, then form the “LLC” with the same name—with the LLC designation replacing the “Inc.” Because this is considered a reorganization under IRC 368-F, it is not a taxable event. The LLC retains the corporation’s original tax ID number and continues to file a corporate tax return.

Circular 230 Disclaimer

The opinions set forth in this material are subject to the disclaimer pertaining to IRS Circular 230 set forth herein.

Unless expressly stated otherwise in this communication, (1) nothing contained in this material was intended or written to be used, can be used by any taxpayer, or may be relied upon or used by any taxpayer for the purposes of avoiding penalties that may be imposed on the taxpayer under the Internal Revenue Code of 1986, as amended; (2) any written statement contained in this material relating to any federal tax transaction or matter may not be used by any person to support the promotion or marketing or to recommend any federal tax transaction or matter; and (3) any taxpayer should seek advice based on the taxpayer’s particular circumstances from an independent tax advisor with

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