Steve Leimberg's Estate Planning Email Newsletter - Archive Message #1471
Date: 30-May-09
From: Steve Leimberg's Estate Planning Newsletter
Subject: **FLASH – Nevada Restricted LLC and LP laws enacted**

Steven J. Oshins is a member of the Law Offices of **Oshins & Associates, LLC** in Las Vegas, Nevada. Steve is a nationally known attorney who is listed in The Best Lawyers in America® and has been named one of the Top 100 Attorneys in Worth magazine. He is one of the most innovative attorneys in the country as demonstrated by how active he has been in writing some of Nevada's most important estate planning and creditor protection laws.

In Nevada's 2003 legislative session, Steve authored the law making the charging order the exclusive remedy of a judgment creditor of a Nevada LLC and LP.

In Nevada's 2005 legislative session, Steve authored the law changing the Nevada rule against perpetuities to 365 years.

Now, hot off the press in Nevada's 2009 legislative session, Steve has been instrumental in the passage of yet another significant law, this one creating the Nevada Restricted LLC and Restricted LP. Steve has created a special web page at http://www.oshins.com/restrictedllcandlp.html with details about the new Nevada Restricted LLC and Restricted LP laws. He can be reached at 702-341-6000, x2 or at soshins@oshins.com. His law firm's web site is http://www.oshins.com .

Steve provides an insider's analysis of the new Nevada Restricted LLC and Restricted LP laws.

EXECUTIVE SUMMARY:

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 now, 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 has now 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.

FACTS:

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.

COMMENT:

WHAT THE APPRAISERS SAY:

The author of this article asked appraisers at two different business valuation appraisal firms ("Appraiser #1" and "Appraiser #2", respectively) to each independently prepare a memorandum responding to certain hypothetical questions posed by the author of this article. Appraiser #1 is Steve Nicolatus (wevc@qwest.net) and Peter Agrapides (panayotiagra@yahoo.com), both of Houlihan Valuation Advisors, in Las Vegas, Nevada and Salt Lake City, Utah. Appraiser #2 is Don Parker (dparker@bizvals.com) of Gryphon Valuation

Consultants of Las Vegas, Nevada.

The questions were asked for the specific purpose of obtaining an estimate of the *additional* valuation discounts that should be available using the Restricted Entities.

The appraisers were specifically told that the author may cite portions of the responses in articles but with the limitation that these are only *estimates* and that they may not necessarily be followed in an actual appraisal requiring more extensive research and an application to actual facts.

Hypothical #1:

The Restricted Entity disallows any Member/Partner distributions for 10 years. Appraiser #1 estimated an additional 10% to 30%+ discount on top of the discount that would be obtained without this additional provision. Appraiser #2 estimated an additional 15% to 35% discount on top of the discount that would be obtained without this additional provision.

Hypothical #2:

The Restricted Entity disallows any Member/Partner distributions for 5 years. Appraiser #1 estimated an additional 5% to 20%+ discount on top of the discount that would be obtained without this additional provision. Appraiser #2 estimated an additional 10% to 25% discount on top of the discount that would be obtained without this additional provision.

Hypothical #3:

The Restricted Entity disallows any Member/Partner distributions for 1 year. Appraiser #1 estimated an additional 3% to 10% discount on top of the discount that would be obtained without this additional provision. Appraiser #2 estimated an additional 3% to 10% discount on top of the discount that would be obtained without this additional provision.

Hypothical #4:

The Restricted Entity disallows any Member/Partner distributions ranging from 1 to 10 years, except to allow all income/growth beyond the capital contributions to be distributed. Appraiser #1 estimated an additional 3% discount for a 1-year restriction to 10% for a 10-year restriction on top of the discount that would be obtained without this additional provision. Appraiser #2 estimated an additional 2% discount for a 1-year restriction to 15% for a 10-year restriction on top of the discount that would be obtained without this additional provision.

Hypothical #5:

The Restricted Entity disallows any Member/Partner distributions ranging from 1 to 10 years, except to allow an amount equal to the highest federal/state income tax to be distributed to eliminate the taxation on phantom income. Appraiser #1 estimated an additional 2% discount for a 1-year restriction to 10% for a 10-year restriction on top of the discount that would be obtained without this additional provision. Appraiser #2 estimated an additional 3% discount for a 1-year restriction to 15% for a 10-year restriction on top of the discount that would be obtained without this additional provision.

THE FUTURE OF VALUATION DISCOUNTS:

The Treasury Department's "Greenbook" was released on May 11, 2009. One of the proposals in the Greenbook seeks to modify the application of IRC §2704(b) such that disregarded restrictions would include restrictions on liquidation of an interest that are measured against standards prescribed in the Treasury Regulations rather than against default state law.

There have been a number of other recent proposals that attempt to curb valuation discounts. It is likely that at some point there will be some changes to our valuation system.

However, the willing buyer/willing seller definition found in the estate and gift tax Treasury Regulations would be disrupted significantly with any modifications that do not reflect real restrictions on business interests. Because of this, there are a number of large groups lobbying against any significant modifications to these laws.

FLEXIBILITY OF THE NEW NEVADA LAW:

Remember that the new Nevada Restricted LLC and LP statutes only create a new 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.

CONCLUSION:

The possibilities are endless. The creative draftsman will design the Restricted LLC or LP around the contemplated transaction. For example, if a non-voting interested in a Restricted LLC is being gifted to a ten-year GRAT, the draftsman might put the ceiling on distributions in an amount just high enough to make the annuity payments each year with all restrictions to be removed at the end of the ten-year period.

HOPE THIS HELPS YOU HELP OTHERS MAKE A POSITIVE DIFFERENCE!

Steve Oshins

CITE AS:

CITES:

Nevada SB 350; NRS Chapters 86, 87A and 88.