A Family Limited Liability Company (FLLC) is a legal entity created to assist your family in accomplishing your estate planning goals and to provide you and your family with better control and asset protection while accomplishing those estate planning goals.

The following are some of the goals of a Family Limited Liability Company:

- Control and manage family business and investment assets
- Protect such assets from personal creditors of a family member
- Protect family members from liability relating to the operation a family business
- Provide management experience for second and third generation family members
- Prevent succeeding generations from acquiring a direct interest in business and investment assets owned by the family
- Prevent fragmentation of family business and investment assets
- Reduce estate and gift taxes
- Allow small gifts without the necessity of deeding small interests in real property
- Consolidate family assets to reduce tax and business reporting requirements

How do You Form a Family Limited Liability Company?
The basic steps in the formation and operation of an FLLC are:

- Create Articles of Organization and an “Operating Agreement” (i.e., a written FLLC agreement) which will meet your particular goals.
- Transfer business and investment assets to the FLLC in return for membership interests. A couple often splits ownership of the Company on a 50/50 basis. A single parent can be the sole initial member of the FLLC.
- The parents then transfer “Membership Interests” in the entity (similar in concept to shares of stock in a family company) to their children, or trusts for their children’s benefit. These transfers are can be made over time on an annual basis.

Estate Planning Benefits of a Family Limited Liability Company
Once properly implemented, the Family Limited Liability Company provides the following benefits:

Control and Management of Family Business and Investment Assets. The greatest advantage of an FLLC is the ability of parents or grandparents to enable younger generation family members to participate in the economic and social benefits of a family’s assets while still maintaining control of the assets. This structure allows junior generations to experience the burdens and benefits of ownership, but nevertheless, be protected by the experienced judgment and guidance of the senior generation.

Estate and Gift Tax Valuation Planning. FLLC’s may reduce the value of the property you own for transfer tax purposes. When the assets are contributed to the FLLC, you convert your ownership of a specific asset into ownership of an interest in the FLLC which holds the asset.

For example:

Parent’s Asset \[\rightarrow\] FLLC
Membership Interest \[\leftarrow\] FLLC
Estate Planning Benefits for FLLC

What does this conversion do? The conversion replaces the asset previously in your estate with a percentage membership interest. This conversion reduces the estate or gift tax value of the asset formerly held outside the FLLC because a membership interest is less valuable than outright ownership of the property itself.

The question raised is: What is the value of the membership interest as compared to the original asset? The factors to consider are:

<table>
<thead>
<tr>
<th>Orginal Asset</th>
<th>FLLC Interest</th>
</tr>
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<tbody>
<tr>
<td>Absolute Control Over the Asset</td>
<td>YES</td>
</tr>
<tr>
<td>Ability to Easily Sell the Asset</td>
<td>YES</td>
</tr>
<tr>
<td>Right to Withdraw the Income</td>
<td>YES</td>
</tr>
</tbody>
</table>

The “no’s” limit the ability of an FLLC member to convert the economic value of the property to cash and therefore, the membership interest is less valuable than the original asset when owned outright. The rationale for the reduction in value from the value of the original asset to the lower value of the membership interest are:

- **Minority Interest Discount:** Reflecting a lack of control.
- **Marketability Discount:** Reflecting the inability to easily sell the original asset because of the terms of the Company's operating agreement.

Example: H owns an asset worth $100,000. H contributes the asset to an FLLC in return for a membership interest.

Assume the terms of the operating agreement are such that the minority interest discount is 15% and the marketability discount is 20%. The calculation of the estate tax value of the FLLC is:

\[
\text{Unrestricted Asset Value} \quad \$100,000
\]

\[
\text{less:} \\
\text{Minority Interest Discount} \quad (15,000) = (.15 \times 100,000)
\]

\[
\text{Marketability Discount} \quad (17,000) = (.2 \times 85,000)
\]

\[
\text{Estate Tax Value} \quad \$68,000
\]

The combined Minority and Marketability Discount is 32%. This same discount is applied to fractional gifts of membership interests.

Example: H gives a 10% interest in an FLLC to his daughter:

\[
\text{Pro Rata Value} \quad (.10 \times \$100,000) \quad \$10,000
\]

\[
\text{less:} \\
\text{Discount (32%)} \quad (3,200) = (.32 \times 10,000)
\]

\[
\text{Gift Tax Value} \quad \$6,800
\]

**Asset Protection Planning**

Asset protection planning with FLLCs includes “inside creditor protection,” “outside creditor protection,” and “litigious family circumstance protection.”

“**Inside Creditor Protection**” refers to protection of the partners from debts and liability claims arising at the Company level. This protection from inside creditors applies to all members, unlike a limited partnership in which the general partners remain jointly and severally responsible for Company debts and claims.

“**Outside Creditor Protection**” refers to protection of the assets held in the Company from creditors of the members in their individual capacities. The protection of the Company’s assets from outside creditors of a member as an individual is primarily the result of the fact that:

- A member has no right of ownership of the Company’s assets and
- A successful attachment or foreclosure by a creditor, does not give member status to the creditor. The creditor’s rights are embodied in a document termed a “charging order” which only allows the creditor to receive distributions to which the debtor member is otherwise entitled.

The combination of the limitations of the member’s access to Company assets and the charging order limitations, protect the Company’s assets from a member’s creditors. The limitations do not cause the creditor to simply “go away,” but will frequently allow a reasonable negotiated settlement.

“**Litigious Family Circumstance Protection**” reflects the fact that when a family’s business and investment assets are held in an FLLC, gifts during life or at death vest membership interests in the donee/beneficiaries and not actual
interests in the assets held by the FLLC. As such, spouses of the members, or others, are unable to attach anything other than the membership interest, which may have little or no value to the adversary.

**Leveraging the Annual Exclusion and Unified Credit**

The term “leveraging” means using combined Minority and Marketability Discounts to give away a greater than $11,000 annual exclusion gift or $1,000,000 unified credit gift, as the case may be. As an example, using a 32% combined discount, a donor may gift a $1,470,588 share of the pro rata value of an FLLC’s property and only use $1,000,000 as the gift tax value of the Company interest.