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Helping Families Preserve and Protect Assets and Values

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THOUGHT YOU'D LIKE TO SEE THIS:

FAMILY LIMITED PARTNERSHIPS

The family limited partnership (FLP) is one of the best-known of all sophisticated wealth-transfer planning devices. Another very similar device is the family limited liability company (FLLC). Although it is certainly not appropriate in every situation, and it must be considered as part of an overall process in conjunction with many other tools and techniques, it is a very important concept that should be considered in most large or rapidly growing estates.

Here is a brief explanation of what FLPs are and who will find them useful.

FLP DEFINED: An FLP is an entity in which the parties are so closely related that they are roughly considered part of the same economic unit. In a typical FLP, parents or grandparents will transfer real estate, publicly-traded securities, an interest in a closely-held business, or some combination of these, or other business/income-producing property, or appreciating assets into a partnership entity.

The transferors will (initially at least) retain both general partnership and limited partnership interests. But at some point, other family members are given or sold (or both) limited partnership interests either all at once or over a period of time.

All parties are bound by an agreement which conforms to state law formalities and clearly defines the general and limited partners' responsibilities and interests as well as the ability to (or restrictions on) transfer their respective interests.

FLP PROFILE: Typically, the client who sets up an FLP will be in his or her early to mid-40s or older, married, have children and/or grandchildren. He or she has business or investments in excess of $5,000,000 (aside from his or her principal residence and life insurance) consisting of a business (or business interest), real estate holdings, and/or a large and diversified portfolio of securities that are appreciating in value. Younger single (divorced, widowed, never-married) individuals with businesses and/or "investment" estates of $3,000,000 or more who are concerned about transferring wealth to someone other than, or in addition, to a charity may find FLPs very appealing.

To be a candidate for an FLP the client must have sufficient tolerance for the aggravation, complexity, and risks involved in the planning, design, formation, and maintenance of the FLP and be willing to pay for competent legal/professional services and appraisals/valuation, and on-going accounting expenses.

Furthermore, the client should have already applied or considered all appropriate "basic" techniques such as: (1) classic will/marital/non-marital trust(s), (2) allocation of ownership of assets between spouses to assure full use of both spouses' unified credit equivalents, (3) irrevocable life insurance trusts, (4) annual exclusion gifts, (5) unified credit gifts — to the extent appropriate and his/her willingness to make lifetime gifts, (6) charitable remainder/charitable lead trusts, (7) grantor retained income/annuity trusts, and (8) revocable living trusts.

Example: Steve and his daughter Lara decide to enter into a business/investment venture together. They would like to operate informally and Steve would like to use the entity to shift both income and wealth to Lara. Steve transfers a building in his name worth $1,000,000 with a basis of $100,000 into a family limited partnership. Initially, he receives all the general and limited partnership interests. Then, he retains a 25-percent interest and gives Lara limited partnership “units” worth 75 percent. He has therefore made a gift to Lara of (for valuation purposes something less than) $750,000 and has retained an interest worth (more than) $250,000. Steve will be the general partner and Lara the limited partner. He may use his available lifetime gift tax exclusion amount to shelter all or part of the gift from current taxation.

ADVANTAGES OF FLPs: Here's a partial list of some of the many tax and non-tax advantages or uses of FLPs:

(1) facilitates wealth and income shifting,
(2) funds spouse's estate tax exclusion,
(3) provides legal reliability,
(4) relatively simple to form or terminate,
(5) provides contractual flexibility,
(6) allows structural flexibility,
(7) facilitates investment flexibility,
(8) enables a consolidation of asset management,
(9) allows creator to maintain significant control,
(10) makes bifurcation of interests possible,
(11) allows both a pass through in general of items of income, deduction, gain, and a net operating loss pass-through,
(12) eliminates ancillary administration and costs,
(13) avoids publicity,
(14) affords a measure of creditor, spousal, and beneficiary protection,
(15) serves as an excellent planning tool for unmarried couples,
(16) has potential for Gift, Estate, GST Tax valuation discounts,
(17) avoids dividend and AMT treatment, and
(18) provides a safe harbor from the transfer for value rules.

If your client wants to bring family members into a business or involve them in a major investment portfolio, and simultaneously improve intra-family communication and reduce friction, at times unavoidable among family members because of their diverging needs, interests, abilities, and opportunities and the client is looking for a vehicle to help educate the junior family members about their investment philosophy and strategies, they should consider an FLP.

AS ALWAYS, PLEASE FEEL FREE TO CALL TO CHAT ABOUT THESE AND OTHER IDEAS THAT MAY ENHANCE YOUR FAMILY'S FINANCIAL SECURITY!

Sincerely,
Weatherby & Associates, PC

Henry C Weatherby