I. **Introduction**[1]

The primary goal of estate planning, apart from passing wealth to the next generation, is to save estate tax. Practitioners save estate tax by using three general techniques: reduce the client's taxable estate while he is alive through inter vivos gifts and other transfers; leave assets in the estate, but in a way that qualifies them for deductions, primarily the marital and charitable deductions; and reduce the value of assets transferred (either inter vivos or at death) through various discounting techniques. Family limited partnerships and limited liability companies are favored because they accomplish both the first and the third objectives: that is, apart from facilitating asset transfers to family members, they may also cause the value of the underlying assets to be discounted for estate tax purposes.

There is a great deal of overlap in the estate planning issues associated with the two types of entities. Both entities are typically taxed as partnerships, primarily because neither entity usually elects out of partnership status under the new "check the box" regulation for entity classification.[2] Because families are typically involved, the family partnership rules of Section 704(e) of the

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[1] For an exhaustive if slightly dated treatment of the issues raised here, *see* KENT H. McMAHAN, WHAT, ME WORRY? – LIMITED LIABILITIY FOR THE OPERATION OF FAMILY BUSINESS IWTHOUT EXTRA TAX COSTS – A COMPARISON OF LIMITED LIABILITY COMPANIES, FAMILY PARTNERSHIPS, AND CORPORATIONS, 12-1 *et seq* (1994 Heckerling Institute on Estate Planning). *See also,* HOWARD M. ZARITSKY, TAX PLANNING FOR FAMILY WEALTH TRANSFERS 10.01 *et seq. (3D ED., 1997).*

[2] Treas. Reg. § 301.7701-3(b) (1998).

Internal Revenue Code of 1986, as amended (the Code) will apply to both entities. Both entities can qualify for certain estate tax valuation discounts, especially those associated with minority interests, lack of control, and lack of marketability.[3]

The biggest difference between FLPs and LLCs is in the area of valuation discounts which are addressed by Chapter 14 of the Code.[4] As the result of Code Section 2704(b) and state law liquidation rights, donors of Massachusetts LLC interests typically receive lesser discounts than donors of Massachusetts FLP interests with similar restrictions. Primarily as the result of the reduced availability of such discounts, most estate planners have not been recommending Massachusetts LLCs except as general partners of family limited partnerships.[5] They have become the entity of choice for real estate lawyers where commercial real estate is involved, however, since they provide total liability protection without compromising beneficial income tax treatment.[6] Unlike Massachusetts, several other states have amended their LLC statutes in an effort to facilitate the same valuation discounts for LLC interests that FLPs enjoy;[7]

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[3] Treas. Reg. § 20.2031-1(b); Rev. Rul. 59-60, 1959-1 C.B. 237, modified by Rev. Rul. 65-193, 1965-2C.B. 370, *amplified by* Rev. Rul. 77-287, 1977-2 C.B. 319.

[4] I.R.C. §2701-2704 (1998).

[5] For a detailed discussion of why LLCs should be sued, *see* Joseph M. Mona, *Advantages of Using a Limited Liability Company in an Estate Plan,* 25 EST. Planning 167 (1998).

[6] G.L.M. c.156C, §22.

[7] Delaware, Oklahoma, Virginia, Oregon, Washington, Georgia, Arizona, and California have all amended their LLC statutes in an attempt to preserve valuation discounts. *See* DEL. CODE ANN. Tit. 6, § 18-603 (1997); OKLA. STAT. Tit. 18, § 63-2036 (1997); VA. CODE ANN. §13.1-1032 (Michie 1998); OR. REV. STAT. § 63-205 (1997); WASH. REV. CODE §

it is likely other states will follow suit, though Massachusetts is not presently anticipated to be one of them.

Family limited partnerships have recently been the subject of Internal Revenue Service attacks in situations where they have been formed to create discounts where none would seem justified.[8] Using its extensive arsenal of statutory and common law arguments, including step-transaction and substance over form, the IRS, in a variety of private letter rulings, has consistently disallowed the discounts where the situations are perceived to be abusive.[9] While the rulings and case law remain a concern, they should not be a problem where there are bona fide business reasons for the formation of the entity.

This article will explore some of the major issues associated with the use of LLCs and FLPs in an estate planning context, including (1) advantages and disadvantages of LLCs and FLPs as compared with other entities, including S-corporations; (2) the family partnership rules and other

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25.15.130 (1997); GA. CODE. ANN. § 14-11-405 (1998); ARIZ. REV. STAT. ANN. § 29-707© (1997); and CAL. CORP. CODE § 17252(a) (1997).

[8] An excellent example of this is the death-bed transfer. In the typical case, the decedent (or more usually her son, pursuant to a Durable Power of Attorney), forms the FLP, transfers her assets into it, and gives away limited partnership interests to her children, all while the decedent is comatose and days away from death. It is hard to fathom how the decedent could form the requisite intent to make a profit, which is the sine qua non of partnership entities – and how estate tax valuation discounts of 40 percent or more can be justified under substance over form analysis. *See* Treas. Reg. § 1.701-2(a) (1994), which codifies the common law principals.

[9] The IRS ruled against taxpayers in Tech. Adv. Mem. 98-42-003 (July 2, 1998); 97-23-009 (February 24, 1997); 97-19-006 (January 14, 1997); 97-25-002 (March 3, 1997); and 97-30-004 involving FLPs, and 97-36-004 (June 6, 1997), involving an LLC. All the rulings cited contain egregiously bad facts.

formation/transfer issues; (3) discounting issues, especially those that arise under Chapter 14 (Sections 2701 through 2704) of the Code; and (4) the focus of recent IRS attacks, especially on FLPs.

II. Advantages and Disadvantages

FLPs and LLCs offer a number of benefits over out-right ownership, both from an estate planning perspective as well as from a general business perspective. First and foremost is liability protection. None of the LLC members, including member-managers, is subject to personal liability.[10] (FLP limited partners should have no personal liability unless they "participate in the control of the business;[11] however, unlike the limited partners, the general partner of the FLFP will have full personal liability. In order to avoid this, the general partner has to be a limited liability entity (typically either an LLC or a corporation) to insulate the partners completely. The assets in the entity are protected from the liabilities of family members as long as the entity form is respected.

The income tax treatment is also advantageous. As long as the entity does not elect out of partnership status, it will incur only a single level of tax and there should be no

[10] G.L.M. c. 156C, §22 (1998). While LLCs are usually discussed as entities which limit the liability of their owners, it is possible that doctrines similar to "piercing the corporate veil" may be applied in an appropriate case.

[11] G.L.M. c. 109, §19 (1998), which lists the actions a limited partner may take without compromising his limited liability status. AS in many other situations, the Delaware limited partnership statute offers the greatest protection for the limited partners. *See* DEL. CODE ANN>, tit. 6, §17-303 (1997), which provides a much broader safe harbor of actions which a limited partner may take without risking personal liability.

tax on formation of the entity unless it is an "investment company" within the meaning of Code Section 721(b). Moreover, if a partner or member should die, the entity can elect to "step up" the basis of its own assets to reflect the estate tax value of the decedent's entity interest pursuant to the provisions of Code Section 754.[12]

From an estate planning standpoint, Massachusetts FLPs, and, to a lesser degree, LLCs, offer numerous advantages over other forms of ownership, including valuation discounts,[13] which will be discussed in greater detail below, and the potential to retain control over the assets in the older (transferor) generation.[14] management can be centralized. Even if the transferor is the manager of the LLC or the general partner of the FLP (or controls the entity general partner), Code Section 2036 should not apply,[15] since the fiduciary duties the partner has and the member/manager may have towards the other owners may be used to render those provisions moot.[16] As long as he does not

[12] *See also,* I.R.C. §§ 743(b) (1998) and § 734(b) (1998). Basis step-up is also available when there has been a sale or exchange of a partner's interest.
[13] If the entities are formed in Delaware rather than Massachusetts, the discounts should be equivalent, as discussed below.
[14] I.R.C. §2036(b)(1998), governing retention of voting rights, does not apply in a non-corporate context.
[15] I.R.C. §2036 provides, in general, that the taxable estate includes assets which were transferred prior to death but in which the decedent retained a lifetime interest.
[16] It should be noted here that the extent of a manager's fiduciary duties to the LLC is open to question and probably limited. Under the Massachusetts LLC statute, G.L.M. c.156C, §7, the Manager may transact business with the LLC as fully as if he were an unrelated party. G.L.M. c.156C, §63(b) (1998) states that, "To the extent that, at law or in equity, a member or manager has duties, including fiduciary duties…" Delaware law contains similar provisions. *See, e.g.,* DEL. CODE ANN. Tit. 6, §§18-107 and 18-1101(1997). If the estate planner intends to rely on fiduciary duties to avoid the applicability of I.R.C. §2036, it

ignore his fiduciary obligations towards his fellow owners and shares distributions in accordance with the ostensible partnership interests, ownership by the younger generation should be respected.[17]

The entities themselves are much more flexible than a trust, which would be subject to the retained life estate provisions.[18] Unlike an irrevocable trust, they can be amended as situations change. Unlike an S-corporation, which is their primary competition, an infinite variety of interests can be created. There is no limit on the number of partners/members, and all types of trusts can own interests.[19] Contrast this with S-corporations, which can have only 75 shareholders, none of whom can be resident aliens. Most trusts will be ineligible to the S-corporation shareholders. While trust ownership of S-corporation stock has been expanded to "electing small business trusts," which were created by the Small Business Job Protection Act of 1996, the income tax rules for ownership by such trusts are almost punitive.[20] Qualified Subchapter S trusts are

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is advisable that those duties be specifically set out in the operating agreement.

[17] But *see* Estate of Schauerhamer, 73 T.C.M. (CCH) 2855 (1997), where the Taxpayer did not make distributions in accordance with the ownership interests and commingled partnership assets with her own.

[18] Specifically, I.R.C. 2036 and 2038.

[19] This may not be as advantageous as it sounds, since the income tax rates on trusts reached 39.6 percent at $8,350 of taxable income in 1998. Frequently, LLC and FLP income is not distributed, even though it is taxed to the trust. Moreover, Tech. Adv. Mem. 97-51-003 (Aug. 28, 1997), which disallowed the use of annual exclusion because the interest had too many restrictions, may raise issues as to whether it is ever advisable to place FLP or LLC interests in marital trusts, which require that all the income be distributed to the spouse.

[20] All the income in such a trust derived from the S-corporation is taxed at the 39.6 percent rate and there is no deduction for distributions to beneficiaries. *See* I.R.C. §§ 1361(e) and 641(d) (1998).

frequently too cumbersome to be useful in a sophisticated estate plan, primarily because they are required to be single beneficiary entities which distribute all their income currently.[21]

FLPs and LLCs are also preferable to S-corporations because of the flexibility of their internal structure. While S-corporations are limited to voting and non-voting common shares which share income and losses equally, FLPs and LLCs can have preferred interests and special allocations, as long as the "substantial economic effect" rules of Code Section 704 are satisfied. Since they are often recommended in an estate planning context, the availability of the Code Section 754 election to increase the basis of the underlying assets also makes them attractive.

As useful as FLPs and LLCs can be, their disadvantages cannot be overlooked. First among them is complexity; the second is cost; and the third is risk. The very flexibility which makes FLPs and LLCs attractive to both tax lawyer and estate planners can also make them more expensive to form and to maintain, since the "standard" provisions are fewer. This necessarily results in increased legal, accounting and bookkeeping fees.

Because these entities are taxed as partnerships, all the various partnership requirements have to be fulfilled.

[21] *See* I.R.C. §11361(d)(3)(1998).

Capital accounts must be maintained;[22] partnership income tax returns have to be filed; the tax allocations in the governing documents must have "substantial economic effect;"[23] and the client has to respect the ownership that the ostensible partnership has established.[24] If the client is likely to misinterpret his right to manage the entity as an unrestricted right of ownership in the entity, it is an inappropriate vehicle to recommend.

Beyond meeting the technical requirements for continued tax viability, the planner has to remain mindful of the effect ownership of the interests will have on the proposed transferees. They are highly inappropriate interests to transfer to charitable remainder trusts, for example, since they generate "unrelated business taxable income,: which will render the otherwise tax-exempt trusts totally taxable.[25] Since FLPs and LLCs are business entities, nonresident alien owners will be taxed on their distributive shares of entity income, which will be deemed to be "effectively connected" with a U.S. trade or business[26] and taxed at graduated rates.

There is substantial confusion over the self-employment tax issues generated by both FLP and LLC interests, and the owners may have trouble allocating a portion of their

[22] Treas. Reg. §1.704-1(b)(2)(iv)(a) (1997).
[23] I.R.C. §704 (1997) and Treas. Reg. §1.704-1(b) (1997).
[24] In Estate of Schauerhamer, 73 T.C.M. (CCH) 2855 (1997), the Donor set up the FLP, and then proceeded to use it as her personal checkbook, never making required distributions and commingling partnership assets with her own. The Tax Court held that the entity was a sham and would not be respected.
[25] I.R.C. 664© 1998).
[26] I.R.C. §871(b) (1998).

distributive shares away from the characterization as self-employment income.[27] This is an area where S corporations have a substantial advantage, since such an allocation is apparently permitted for them.[28] If a substantial portion of the owner's income will be derived from the entity, the self-employment tax issue necessarily becomes more important.

LLCs have their own peculiarities. Debt that is recourse as to the entity may not be included in the basis of the LLC interest for the individual members.[29] Certain favorable Massachusetts excise tax provisions (for example, the exemption of corporate personal property from the calculation) may not be available.[30] Since they are not familiar entities in the capital markets, LLCs may be inappropriate vehicles to recommend if the entity anticipates a public offering.[31] Last, at least in foreign jurisdictions, LLCs may not even be recognized. Tax

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[27] I.R.C. §1402(a)(13) (1998) is the governing statute, but interpretive regulations for LLCs and FLPs have already been proposed and effectively withdrawn on two separate occasions. For a comprehensive analysis of the self-employment tax issues as applied in the context of FLPs and LLCs, *see* Donald C. Alenander, *Pass-Through Entities and Employment Taxes,* 1 BUSINESS ENTITIES 20 (1999).

[28] Durango v. U.S., 70 F.3d 548 (9th Cir. 1995).

[29] Treas. Reg. §1.752-2(b) (1992). For a comprehensive analysis of the basis issues that arise in the context of debt owed by LLCs, *see* Richard W. Harris, *Impact of Liabilities on Members' Basis in Their LLC Interest,* 4J. LIMITED LIABILITY COMPANIES 107, 111 (1997).

[30] *See, e.g.,* G.L.M. c.63, §30 (1996).

[31] This has become less of an issue since November 10, 1997, when the Securities and Exchange Commission issued its no action letter in the Matter of Peapod, Inc. SEC No-Action Letter, [1997 WL 7064422 (S.E.C.)] (November 10, 1997). In that ruling the SEC took the position that limited partners of a limited partnership and shareholders of its corporate general partner could "tack," under Securities Act Rule 144(d), their holdings periods for their limited partnership interests and shares, respectively, onto their holding periods for the shares of Peapod received in a conversion (and, in the case of the general partnership's owners, the general partnership's subsequent liquidation).

treaties usually do not mention LLCs, so the tax results for foreign operation may be open to question.

The risk factor cannot be ignored. The IRS has recently put FLPs in its sights, especially those FLPs that are perceived to be abusive.[32] Transfers involving a comatose donor or personal use property, such as vacation homes, have typically been invalidated as shams, with the attendant interest and penalties, apart from the additional tax. Moreover, recent budget proposals have suggested eliminating the discounts these entities provide for any but active businesses. In its ever vigilant search for new revenue sources, both Congress and the Internal Revenue Service remain mindful of the billions of dollars that will pass as the World War generation dies off, and they continue to seek their share.

III. Some Scenarios

It may be helpful here to describe two scenarios where FLPs and LLCs may be suggested. In the first, the client owns numerous pieces of rental property in the Commonwealth. His two sons, both adults, are both involved in the business. All the real estate is owned in his individual name or in realty trusts of which he or his revocable trust is the sole beneficial owner. One or more of the properties may be

[32] *See, e.g.,* Tech. Adv. Mem. 97-19-006 (Jan. 14, 1997). (Decedent on life-support at time entity formed). The same "substance over form" principles which invalidate abusive FLPs would apply to LLCs; nevertheless, because the latter have not been promoted to the same extent, they may be below the Service's radar, at least for the time being.

contaminated. This is a situation where both entities make a great deal of sense, since the client would be able to limit his personal liability while creating a vehicle to facilitate gifts to his sons. As long as he does not create these entities when he is on his death-bed, either entity should be respected for estate and gift tax purposes, and the attendant discounts, typically 30 percent or more, should be sustained.

In the second scenario, the client, whose assets include her $800,000 principal residence, $200,000 vacation home, and a $3 million stock portfolio, is comatose and her death is imminent. Her accountant in response to entreaties from her children, calculates that the estate tax would be around $1.6 million. Having heard about FLPs, he advises the client's son to form an FLP, contribute the client's stock portfolio and vacation home to it, and give away some percentage of the limited partnership interests to the children, all pursuant to a Durable Power of Attorney which does not authorize either the making of gifts or the formation of business entities. He suggests that the two children contribute $20,000 each of their own low basis stock to make the transaction appear more legitimate. He claims this arrangement, set up within weeks of the decedent's death, will result in a valuation discount "of at least 50 percent" for assets in the partnership, saving the family at least $900,000 in estate taxes. This arrangement probably will not work, since there is clearly no "business

purpose" to the formation of the entity. Moreover, the transfer of low-basis stock t other entity will generate a substantial income tax, since the partnership will be treated as an investment company within the meaning of Code Section 721(b).

IV. Requirements for Partnership Formation

Before recommending an FLP, which is the more favored vehicle in Massachusetts because of the significantly greater discounts it may provide, the estate planner has to ask himself whether there is truly a bona fide business purpose to the entity. If it is likely that the formation of the entity, the transfer of interests to the children, and the subsequent death of the donor will be close in time, the risk that the IRS will collapse the entity is substantial.[33] These are also inappropriate vehicles for personal use property, such as the principal residence and the family's art collection, especially if it will continue to grace the living room walls.[34] If there is no business purpose, the IRS's positions based on case law and Code Sections761 and 701 may negate all the good work the planner has done, and could have the totally untoward effect of giving him a disgruntled client if he has not adequately disclosed the risks of his proposed strategy.

[33] *See, e.g.,* Tech. Adv. Mem. 98-24-003 (July 2, 1998); 97-19-006 (Jan. 14, 1997); 97-23-009 (Feb. 24, 1997);; 97-25-002 (March 3, 1997); 97-30-004; 97-35-003 (May 8, 1997); and 97-36-004 (June 6, 1997).

[34] It should be noted here that LLCs and FLPs are sometimes used for personal use property if the object is not estate tax savings but simply to maintain family control over the assets and to prevent their subdivision and segmentation.

In the second scenario outlined above, it is difficult to see where the "business purpose" is contained, especially if the client has become incapable even of thought. Yet absent imminent death, the creation of an FLP to manage a stock portfolio can have a business purpose of managing the portfolio simply looks a lot more like a testamentary disposition than management of a business property would, especially where the other limited partners have no special expertise beyond spending the dividends. At a minimum, the discounts will be far closer to 10 percent than the 50 percent claimed in the second scenario, reflecting the high liquidity of the underlying assets.

If the business purpose to formation is justifiable, as it is in the first scenario, then, since families are involved, the family partnership rules of Code Section 704(e) must be satisfied. Under this section, to be respected as a partnership capital must be a material income producing factor and the child/partner must be the real owner of the interest in that capital. What this means in practice is that minors are typically not respected as partners, unless they are exercising real ownership rights or own their interests beneficially through a trust.[35]

The regulations under Code Section 704(e) codify the facts and circumstances that the Service will look at in

[35] Michael D. Mulligan, *Dealing with the IRS' Arguments Against Family Limited Partnerships,* 26 ESTATE PLANNING 195 (1999).

determining whether the putative donee really owns the interest that was transferred to him.[36]

The regulations under Code Section 704(e) codify the facts and circumstances that the Service will Look at in determining whether the putative donee really owns the interest that was transferred to him.[37] In essence, the issue is the extent of control the donor has retained and whether that control conflicts with the ostensible ownership. For example, the Service looks at whether there been a retention of income beyond the reasonable needs of the business; whether the financial incentives are such that the limited partners cannot sell or withdraw without financial detriment; whether management controls are inconsistent with normal business operation; and last, whether there has been a retention of control of assets essential to the partnership operation (for example, through retention of assets leased to the partnership).[38]

Even if the family partnership rules appear to be satisfied, recent IRS attacks may raise questions about the tax treatment of a gift of an interest in the entity, at least where the interest has been significantly restricted. In Technical Advice Memorandum 97-51-003, the IRS determined that the gift of a limited partnership interest did not qualify for the gift tax annual exclusion as a present interest gift because the Donor retained too many rights in

[36] Treas. Reg. §1.704-1(e)(2)(ii)(1997).
[37] Id.
[38] Treas. Reg. § 1.704-1(e)(2)(ii)(1997).

the partnership (e.g., income could be distributed to the Donor/parent for any purpose, the limited partner could not transfer his interest, etc.), thereby giving a future, rather than a present interest to the Donee.[39] While the ruling is questionable on its face, since it is the transfer, not the asset, that needs to qualify under Code Section 2503(b), it suggests that the IRS will look beyond the interest that has been transferred if it sees the transaction as too aggressive. Taken to its logical conclusion, this ruling may raise questions as to whether an FLP or LLC interest should ever be an asset of a marital deduction trust, since "all the income" of the FLP or LLC is typically not distributed.

The tax rules governing the income tax treatment of the entity may conflict with the rules to maintain limited liability. Pursuant to the regulations under Code Section 469,[40] a limited partner who participates in the business for more than 500 hours per year is not subject to the passive loss rules, which losses for any but active partners. Yet the limited partner who is able to avoid the passive loss rules may be setting himself up for liability, since, even under the Delaware statute, he cannot become too actively involved in the business. It is not clear whether an LLC member is required to perform such services to avoid the

[39] The loss of the annual exclusion may be far outweighed by the benefits of making a gift whose value has been significantly depressed, however.
[40] I.R.C § 469(h)(2) (1998); Temp. Treas. Reg. § 1.469-5T (1996).

passive loss rules;[41] even if he does, he should not trigger personal liability by doing so. This may be a major advantage of LLCs over FLPs, especially for the client whose beneficiaries are active in the business, as they are in the first scenario.

It has been suggested that the "at risk" rules contained in Code Section 465 may also favor LLCs, at least where the underlying asset is real estate which is financed with what becomes qualified nonrecourse debt.[42] Briefly, partners and LLC members can only deduct losses attributable to their partnership interests to the extent they are at risk. In the LLC, qualified nonrecourse financing is included in basis for the purpose the at risk rules, since no member is personally liable for the entity's debts.[43] In effect, recourse debt can become qualified nonrecourse debt when the property is contributed. This would not be the case with the FLP interest, since the general partner would remain personally liable.

In general, neither the entity nor its partners/members will recognize gain on contribution of property to the partnership.[44] The major exception, apart from debt-financed property, is triggered if the entity is treated as an investment company within the meaning of Code Section 721(b). Transfer of appreciated stock to a partnership 80

[41] Louis A. Mezzullo, *Family Limited Partnerships and Limited Liability Companies,* 812 TAX MANAGEMENT PORTFOLIO (BNA) A-37 (1999).
[42] *See* Scott E. Friedman and James G. Sciarrino, *Estate Planning Vehicle of Choice for the 1990's: FLLLC or FLP?,* 4J. LIMITED LIABILITY COMPANIES 91, 97 (1997).
[43] I.R.C. § 465(b)(6).
[44] I.R.C. § 721(a) (1997).

percent of which consists of publicly-traded securities will trigger a gain to the contributing partners if it results in diversification.[45] Apart from the fact that the transaction proposed in the second scenario looks like a sham, the contribution of the securities will result in a gain for income tax purposes. Had the children not made their own contributions, which exceed the informal 1 percent de minimis level, the investment company rules would not have applied, since there would have been no diversification.

Once the entity is validly formed, it will be taxed as a partnership for federal purposes unless it elects out of partnership status pursuant to the "check the box" regulations,[46] which became effective Jan. 1, 1997. The state tax treatment of FLPs and LLCs has become somewhat simpler since Massachusetts amended its tax laws so that, with noted exceptions, it would follow the Internal Revenue Code as in force on Jan. 1, 1998.[47] As noted in Technical Information Release 97-8, Massachusetts will also follow the federal classification for single member LLCs, which are not available under Massachusetts law, as well as foreign LLCs.[48] Surprisingly, the tax classification of other unincorporated entities, such as FLPs, is still governed by Massachusetts, as opposed to federal, law.[49]

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[45] I.R.C. §§ 721(b) (1997) and 351(e) (1998); Treas. Reg. § 1.351-1(c)(1) (1996).
[46] Treas. Reg. § 301.7701-3(b) (1998).
[47] G.L.M. c.62, §1 (1998).
[48] G.L.M. c.62 §17 (1998).
[49] Tech. Info. Rel. 97-8 (June 16, 1997).

Even though the entities are usually classified the same for both Massachusetts and federal income tax purposes, there are differences. Although Massachusetts has now conformed its depreciation rules to the federal system even if it ultimately results in a negative Massachusetts basis,[50] the capital gain calculation will still be made using the Massachusetts numbers.[51] This has implications for more transactions than sales. Under Code Section 704(c), appreciated property which is distributed to another partner within seven years after its contribution triggers gain to the contributing partner. For Massachusetts purposes, that gain is calculated using the state, rather than the federal, basis.[52] Since basis continues to be calculated pursuant to Chapter 62, Section 6F,[53] there is some question how the Code Section 754 election would operate.

The basis issue can arise in surprising ways. For federal purposes, property jointly owned by a husband and wife where one party has died receives a step-up in basis for only 50 percent of the value if the joint tenancy was created after December 31, 1976, pursuant to the provisions of Code Sections 2040(b) and 1014. If it was created before that date and the decedent contributed the entire consideration, the basis step-up can be 100 percent.[54] For Massachusetts purposes, the basis is stepped up only for 50

[50] Tech. Info. Rel. 98-15 (December 23, 1998).
[51] G.L.M. c.62, §6F (1998).
[52] *Id.*
[53] Tech. Info. Rel. 88-7 (July 5, 1988). *See also,* 830 C.M.R., §62.4.1.
[54] Gallenstein v. U.S., 975 F.2d 286 (6th Cir. 1982).

percent of the value, irrespective of when the tenancy was originally created.[55]

In contrast to the federal system, Massachusetts also does not allow net operating loss carryovers or carrybacks, or a Schedule A deductions.[56] Unlike the federal system, there is no recapture of excess depreciation, which is simply treated as capital gain.[57] In future years, Massachusetts may again diverge significantly from federal treatment, since very few Code changes will be continually incorporated into Massachusetts law.[58]

V. Discounts

FLPs and, to a lesser degree, LLCs, are utilized primarily because they provide significant discounts from outright ownership of the underlying assets. There are primarily two categories of discounts available: those attributable to the transfer of the asset to the entity, and those derived from the terms of the interest in the entity itself. The first set of discounts – typically those for minority interest, lack of control, and lack of marketability – are common to FLPs and LLCs, as well as to corporations. Using the "willing buyer/willing seller" paradigm described in the regulations under Code Section

[55] Treat v. Commissioner, CCH State Tax Reporter 2 Massachusetts 400-501 (Appellate Tax Board 1998).
[56] Instructions to 1998 Form 3.
[57] Tech. Inf. Rel. 97-3 (March 14, 1997).
[58] The only ones are those associated with Roth and education IRAs, gain on the sale of a principal residence, trade or business expenses, travel expenses, meal and entertainment expenses, and the maximum deferral amount of the deferred compensation plans of government employees. *See* Tech. Info. Rel. 98-1 (Oct. 6, 1998).

2031,[59] it is clear that a buyer would pay less for a noncontrolling interest in an entity that owns an asset, than he would pay for an undivided minority interest in the same asset. Indeed, the only discount the IRS typically allows on undivided interests in real estate, is that attributable to the petition to partition.

The more interesting issue for estate tax purposes is the discount attributable to the terms of the interest itself, which are addressed in Chapter 14 (Code Sections 2701-2704). The Chapter 14 valuation rules, especially Code Section 2704(b), are the primary reason that estate planners using Massachusetts entities are recommending FLPs rather than LLCs. The allowable discounts are simply greater.[60]

In order to understand what Chapter 14 does, it is useful to understand what preceded it and its now repealed predecessor, Code Section 2036(c). A client with a profitable business, but ready to retire, would be advised to recapitalize his company. For his common stock, he would receive preferred stock, which he would retain, and common stock, which he would give away. The overall idea at the time of the recapitalization would be to make sure

[59] Treas. Reg. § 20.2031-1(b) (1965) provides that property in an estate will be valued at its fair market value on the date of death or alternate valuation date. Fair market value is then defined as, "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts…"

[60] This appears to be changing in other states, depending on whether the applicable LLC statute has been amended to preserve the discounts. In addition to Mona, cited at footnote 5, above, *see* Scott E. Friedman and James G. Sciarrino, *Estate Planning Vehicle of Choice for the 1990's: FLLC or FLLLP?,* 4J. LIMITED LIABILITY COMPANIES 91 (1997).

that the preferred would be deemed to have a value of the business, so that the gift tax cost of giving away the common would be negligible. This was easy to accomplish under Code Section 2031: the preferred was given both liquidation preferences nearly equal to the value of the equity at the time of the recapitalization, as well as a very high dividend yield (frequently upwards of 20 percent). Coupled with various other commercially questionable options and rights, these preferences made a high stock valuation easily justifiable.

When the founder died, the alchemy of tax planning worked its magic, fort the preferred would typically have far less value than its share of the equity and control and even less than it did when the recapitalization took place. First, the generous dividend had been eliminated. Second, the founder's interest would be subject to a (low price) buy-out agreement. Third, the terms of the interest, including the elective options and rights which supported the value had now disappeared. Billions of dollars in assets were thus transferred to the younger generation at significantly reduced transfer tax cost.

Congress belatedly recognized that the Code Section 2031 paradigm of willing buyer/willing seller was inappropriate in the family context, since the estate tax provided significant incentives to depress the value of the asset that was being transferred. The response was Chapter 14, which reversed the normal valuation results by ignoring

questionable value-depressing terms. Under Code Section 2701, Congress allocated transfer tax value in a recapitalization to the common that was given away, rather than to the preferred that was retained, unless the preferred complied with the strict limitations of that section. Under Code Section 2703, buy-out agreements and similar provisions would now be ignored unless they were bona fide business arrangements. Under Code Section 2704, restrictions on liquidation and withdrawal rights which had been drafted primarily to support lower estate tax values, would be ignored if they were more restrictive than the default provisions of the applicable state law.[61]

The power to liquidate an interest is obviously an important factor in valuing that interest, and any lapse of a right to liquidate an interest would necessarily depress the value of it. Before the advent of Chapter 14, donors had simply allowed the various rights which supported the value of the preferred at the time the common was given away, to lapse, thereby increasing the value of the common without incurring a gift tax cost. Under Code Section 2704(a), the lapse of either a voting right or a liquidation right will now be treated as a (taxable) transfer by the holder of that right.[62] Since the value of the common has been increased as the result of the action

[61] I.R.C § 2702 (1998), not relevant here, deals with grantor-retained income trusts, grantor-retained annuity trusts, grantor-retained unitrusts, qualified personal residence trusts, and other entities which split ownership of the asset into term, life and remainder interests.
[62] *See* Treas. Reg. § 25.2704-1 (1998), under which a right is treated as lapsed if its present exercise is restricted or eliminated.

of the donor, the donor has effectively made a gift, and he will be charged with the attendant gift or estate tax cost.

But Congress went farther than simply addressing lapsing rights. It was apparent that certain terms in the entity that was created – either the LLC operating agreement, or the FLP partnership agreement – could also have the effect of depressing value. Since there would be no rights that lapsed in such a case, Congress looked to what state law would have provided for the interest in the absence of a governing document. Under Code Section 2704(b), any "applicable restriction" will be disregarded in valuing the transferred property where the transfer is made to a member of the transferor's family and before the transfer the transferor and his family control the entity. Applicable restriction in this context will include provisions in the operating agreement or limited partnership agreement which give fewer liquidation rights than what state law provides.

In effect, the minimum transfer tax value of the interest is now determined by the state law default provisions, not by the actual governing documents. Consequently, the liquidation/withdrawal restrictions of a Massachusetts FLLC are less effective in depressing the value of the transferred interest than the same restrictions applied in the Massachusetts FFLP context because the state law defaults give the LLC member greater rights. Under the state law default, the withdrawal of a

limited partner does not dissolve the entity, whereas the withdrawal of an LLC member does. Wh3ether or not eh donor limits the beneficiary's rights through the operating agreement, the transferred interest is valued as if the beneficiary retained the state law liquidation right – i.e., close to t he value of the underlying asset, as adjusted by the entity-related discounts.[63]

The specific statutory provisions may clarify this concept. General Laws Chapter 156C, Sections 32 and 33 give the withdrawing member the "fair value" of his LLC interest. Under Section 36, the member can withdraw on six months' prior notice, thereby dissolving the LLC under Section 43. In effect, the state law default allows the member to reach the underlying assets simply by withdrawing and dissolving the entity. Since he is able to reach the underlying assets by withdrawing, his interest is valued with fewer discounts.

For the Massachusetts limited partner, however, withdrawal of the limited partner does not dissolve the FLP.[64] Moreover, although the limited partner can withdraw on six months' prior notice, all he is entitled to is the value of his interest in the limited partnership "based upon his right to share in distributions from the limited partnership" – i.e., discounted going concern value, not liquidation value. This is the transfer tax value irrespective of what the actual value might be because of

[63] Treas. Reg. § 25.2704-2(b) (1998).
[64] G.L.M. c.109, §44 (1998).

additional restrictions contained in the partnership agreement.

The impact of these provisions from an estate planning standpoint is that the planner using only Massachusetts entities would clearly choose the FLP over the LLC wherever discounts are the primary concern. The ability of a Massachusetts LLC member to withdraw and thereby to dissolve the LLC means that there is really no impediment to his receipt of the underlying assets – and therefore, that his interest in the LLC should be valued very close to the value of those assets. If the client in the first scenario chooses an LLC, the liquidation value of the buildings owned by it, which the LLC member would receive on dissolution of the LLC, has to be greater than the discounted cash flow value of rents which his withdrawal from an FLP owning the same assets would give him.

Even better for discount purposes than the Massachusetts limited partnership act, is that in Delaware.[65] Since the overriding rule is freedom of contract, many more value-depressing provisions can be added without adverse estate tax consequences. Unlike the Massachusetts statute, Delaware does not allow the limited partner to withdraw unless the partnership agreement gives

[65] *See* Tech. Adv. Mem. 97-35-003 (May 8, 1997) for a detailed discussion of the Massachusetts statute in the context of the elimination of the right of withdrawal as an "applicable restriction" under I.R.C. § 27704(b). This ruling graphically illustrates why sophisticated planners prefer to form these entities under Delaware, rather than Massachusetts, law.

him that right.[66] Since the limited partner can be precluded from withdrawing, he can effectively be precluded from realizing substantial value for his interest. And if he is given the right to withdraw, he is only entitled to the fair value of his interest in the partnership "based upon his right to share in distributions from the limited partnership."[67] These provisions have the effect of depressing the value of the interest even further. Coupled with the significantly greater safe harbor liability protection in Delaware, Delaware has become the situs of choice for these entities.

Delaware has amended its LLC provisions so that members will receive similar discounts to the owners of limited partnership interests. Pursuant to Section 18-603, an LLC member "may not resign from a limited liability company prior to the dissolution and winding up of the limited liability company." And if he is able to withdraw, all he receives for his interest is fair value" based upon [his] right to share in distributions from the limited liability company.[68] Since these provision are very similar to those contained in Delaware's limited partnership act, it is likely the discounts should also be similar. In the first scenario described above, it is likely the client will prefer the Delaware LLC, since he should obtain equal

[66] Del. Code Ann. tit. 6, § 17-603 (1997).
[67] Del. Code Ann. Tit. 6, § 17-604 (1997).
[68] Del. Code Ann. Tit. 6, § 18-604 (1997).

discounts without being forced to form a second entity to act as general partner to avoid personal liability.

VI. IRS Attacks and Code Section 2703

FLPs and their attendant discounts are currently the subject of close IRS scrutiny, at least where the business purpose to formation is questionable. In attacking FLPs, the IRS asks first, is the FLP a real partnership – i.e., do the partners intend to produce and to share profits? The IRS uses the family partnership rules of Code Section 704(e) and the definition of partnership under Code Section 761 to attack entities that may not pass muster. In general, the questions are, (1) is there a business purpose, and (2) is the business purpose bona fide?

The determination of the existence of an actual partnership is a facts and circumstances test. The IRS looks at a number of factors, including the reason the partnership was formed; age and health of donor; whether the partnership form is respected; receipt of actual income distributions by the ostensible partners; recognition of limited partners in conduct of partnership business; extent of donee's power over his interest (can he dispose of it); experience level of donees; and compliance with the various statutory requirements of the entities created.[69]

It is clear that the client in the first scenario outlined above has a business purpose, since he has an

[69] *See, e.g.,* Tech. Adv. Mem. 97-23-009 (February 24, 1997); 97-19-006 (January 14, 1997); 97-25-002 (March 3, 1997); and 97-30-004 (April 3, 1997).

ongoing business which needs to be managed. If his sons were simply employees, he would probably need to give them an equity stake both to motivate and to retain them. Moreover, he is subject to personal liability the way the assets are held; he would choose some type of limited liability entity simply to decrease his exposure.

Contrast this with the second scenario, where the life expectancy of the donor is so short. As would be expected, judicially developed doctrines of substance over form and step transaction have been used successfully by the IRS to disregard the existence of the FLP in similar cases. For the IRS, as it should be for practitioners, the issue is whether the formation of the partnership, transfer of partnership interests, and the decedent's death are so close in time that the combined transactions should be treated as one testamentary transfer whose primary if not exclusive motive is tax avoidance. Where the facts are egregious, the IRS has been relentless in disallowing the discounts.[70] Its primary precedential support for this analysis is *Estate of Murphy,*[71] and *Estate of Cidulka,*[72] both of which were cases involving transfers of closely held stock. The transfers, which appear to have been made to support minority interest discounts after death, were simply ignored.[73]

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[70] The IRS ruled against taxpayers in Tech. Adv. Mem. 98-42-003 (July 2, 1998); 97-23-009 (Feb. 24, 1997); 97-19-006 (Jan. 14, 1997); 97-25-002 (March 3, 1997); and 97-30-004 (Apr. 3, 1997) (involving FLPs), and 97-36-004 (involving an LLC).
[71] 60 T.C.M. (CCH) 654 (1990).
[72] 71 T.C.M. (CCH) 2555 (1996).
[73] *But see,* Estate of Frank, 69 T.C.M. (ch) 2255 (1995), WHERE THE Tax Court reached the opposite conclusion on similar facts.

Unfortunately, the IRS does not limit itself to its statutory and common law weapons. In Florida, Illinois, North Carolina, Connecticut and Rhode Island, the IRS audit questionnaire asks about the professional who recommended the entity be formed, and whether he had lectured to any group about the benefits of FLPs. In Technical Advice Memorandum 97-30-004, the IRS disregarded the FLP where the decedent's son had written an article on the benefits of FLPs, and the father had listed in an ancillary statement the same non-tax business reasons for the FLP as the son had listed in the article. Given the hype that has surrounded FLPs (and their persistent recommendation by accountants and other nonlawyers in situations where the validity of their use is highly questionable), this result was to be expected, especially in light of the lack of an actual business purpose.

Had the IRS limited itself to attacks based on case law, or even an analysis of the background of the person how had recommended the FLP, estate planners probably would have been a bit annoyed, but still comfortable. As they say on Wall Street, the pig rule still operates, and any professional foolish enough to violate it deserves what he gets.[74] The problem is, the IRS has recently used Chapter 14 (specifically, Code Section 2703(a)), to attack FLPs in situations where the statute was clearly not meant to apply.

[74] The pig rule states, "Bears make money, and bulls make money, but hogs get slaughtered."

To review, Code Section 2703(a)(2) provides that the value of any property is generally "determined without regard to…any restriction on the right to sell or use such property." The provision's intended impact is to ignore restrictions on transfer of the interest (e.g., sections of the partnership agreement/operating agreement containing mandatory buy-back provisions, options to purchase, rights of first refusal and the like) in valuing the interest. The rule is not a blanket elimination of the valuation impact of these rights; rather, the exception to it contained at Code Section 2703(b) makes it clear that bona fide business arrangements will be respected for valuation purposes.

In its overzealous attempt to r5each situations that were already reachable, the IRS simply redefined the word "property" under the statute.[75] Rather than interpreting the word "property" to mean interests in the partnership, LLC or corporation, which was the common understanding of the provision, the IRS said that the word "property" meant the underlying assets – and that the entire partnership agreement itself became the restriction on transfer addressed by the statute. As the IRS stated,

> Had the decedent, under the terms of her testamentary instruments, directed the creation of a partnership funded with her assets at her death, and bequeathed the partnership interest to her children, it is clear that the assets would be

[75] Tech. Adv. Mem. 97-19-006 (Jan. 14, 1997).

> valued for estate tax purposes without regard to the restrictions resulting from the decedent's imposition of the partnership…. [T]he estate cannot avoid this result by attempting to cover the decedent's assets with a partnership wrapper prior to her death, solely to reduce estate taxes. The steps of the transaction.. should be collapsed and viewed as a single integrated transaction: the transfer at her death of the underlying partnership assets subject to the partnership agreement… Thus, the partnership assets are properly viewed as the subject matter of the transfers. Any reduction in value of the underlying assets caused by the partnership agreement is disregarded under Section 2703(a)(2) in determining the value of the transfers.

Under the IRS analysis, the vast majority of estate planning can be disregarded, simply because the action taken has the effect of reducing the estate tax. If one takes this reasoning to its logical conclusion, annual exclusion gifts can be ignored, simply because they would have been included in the decedent's estate had she made them at her death. Such a result is absurd. Moreover, if the partnership agreement itself is the restriction subject to the statute, then there would have been no need to have passed Code Section 2704(b), which analyzes the restrictions

in the partnerships/operating agreement in the context of state law default provisions. If the whole partnership agreement is void, why do its individual provisions need to be analyzed?[76] The analysis sent chills down the spines of estate planners. Unfortunately, it has been used in other rulings as well.[77]

In analyzing these rulings estate planners nurtured a hope that the IRS would retreat from its aggressive and highly questionable legal positions. The rulings themselves have no precedential value,[78] but do indicate the IRS's current interpretations of the statute. Unfortunately, the IRS has reaffirmed its position in Technical Advice Memorandum 98-42-003. As with the other rulings, over 98 percent of the value of all partnership assets were transferred in the six weeks preceding the decedent's death, which raised questions of the real purpose behind the transfers. The IRS ruled that Code Section 2703(a) applied, as follows:

> Under section 2703(a)(2), the value of the "property" transferred is determined without regard to any restriction relating to the "property". In the instant case, we believe the "property" subject to Decedent's transfers was the underlying partnership property. Any reduction in

[76] For a comprehensive analysis of the IRS use of I.R.C. §2703, *see* John A. Bogdanski, *Family Limited Partnerships: Meet Section 2703,* 24 EST. PLANNING 235 (1997).
[77] *See, e.g.,* Tech. Adv. Mem. 97-25-002 (March 3, 1997).
[78] I.R.C. §6110(j)(3) (1998).

> value of the underlying assets caused by the partnership agreement is disregarded under section 2703(a)(2) in determining the value of the transfers. The steps of the transaction… should be collapsed and viewed as a single integrated transaction: the transfer at her death of the underlying trusts assets subject to the partnership agreement. [Citations omitted]

The IRS went on to analyze the partnership interests themselves as subject to restrictions on transfer which could be disregarded. The IRS looked at the impediments to transfer that the partnership agreement imposed – limited ability to withdraw or retire from the partnership, inability to dissolve or terminate the partnership – and concluded that those restrictions themselves, which are common to most partnership agreements, fall under Code Section 2703(a)(2) and therefore should be disregarded.

As alternative grounds for disallowance of the discounts, the IRS also used more common grounds, including (1) that the transfer to the partnership constituted a gift subject to the gift tax; (2) the provisions in the partnership agreement prohibiting the decedent from liquidating her interest constitute an "applicable restriction" within the meaning of Code Section 2704(b), which should be disregarded; or (3) substance-over-form, step-transaction analysis. If there is any comfort in this ruling, it may be contained in the fact that the transaction

itself was abusive, and the IRS intended to reach it however it could. As the IRS put it,

> It is inconceivable that Decedent would have accepted, if dealing at arm's length, a partnership interest purportedly worth only a faction of the value of the assets she transferred. This is especially the case given the Decedent's age and health, because it was impossible for her to ever recoup this immediate loss. Further, it is inconceivable that Decedent (or her representative) would transfer such a large portion of her liquid assets to a partnership, in exchange for a limited interest that terminated her control over the assets and their income stream, if there other partners had not been family members…. We believe it is clear that the primary, if not the sole, purpose of the partnership was to artificially depress the value of Decedent's assets for a brief period as the assets passed through Decedent's estate to her children. Applied within the context of section 2703(a)(2), which focuses on restriction on the right to sell or use property, we believe that a "device" under section 2703(b)(2) is reasonably viewed as including any restriction that has the effect of artificially reducing the value of the transferred interest for transfer tax purposes

without ultimately reducing the value of the interest in the hands of the transferee-family member. We believe the partnership arrangement, under the circumstances presented, satisfies this description.

The question practitioners must ask is whether this imposition of judicially defined doctrines onto the language of Code Section 2703(a) is really that radical. If the "restriction" is measured against the standard of "substance over form," there is nothing particularly disturbing about it, since the common law of tax clearly exists in the interstices of the statute.[79] If, on the other hand, a nonabusive partnership agreement really is the restriction on transfer which the statute is addressing, family limited partnerships may be risky, at least until the courts have spoken. At a minimum, these rulings make it advisable for practitioners to inform their clients of the potential exposure, even if case law ultimately invalidates the IRS's positions.

VII. **Conclusion**

Even without the transfer tax discounts that LLCs and FLPs afford, there remain ample business reasons for their

[79] In Tech. Adv. Mem. 98-08-010 (Nov. 13, 1997), involving the prospective tax implications of transfers to an FLP, the Service declined to rule on whether I.R.C. Section 2703(b) applied, on the grounds that this would be a factual determination. Pursuant to the standards set forth in Rev. Proc. 1999-1, 1999 I.R.B. 6, the Service does not rule on factual matters. By relying on the facts, the Service may be indicating that the partnership agreement would constitute a restriction only if it were not bona fide. This could be good news, at least for practitioners whose clients are not at death's door. Of course, the Service may also be waiting to see what happens when this issue gets to court.

use. As has been cogently pointed out elsewhere,[80] LLCs and FLPs allow the older family members to retain control over management of the entity's assets, to restrict subsequent transfers of the interests in the entity, and to undo the entity without unfavorable income tax consequences if circumstances should change, none of which could be done with an irrevocable trust. Second, they reduce expenses and facilitate transfers of interests, while at the same time avoiding ancillary probate for out-of-state real estate owned by the entity. Third, the owners can avoid personal liability if an LLC or an FLP with an entity general partner is used for contaminated assets. Fourth, the assets themselves can be shielded from the creditors of the donees as well as the donor. Last, they create a vehicle with which to educate the younger generation about asset management.

From an estate tax standpoint FLPs and, to a lesser extent, LLCs, offer a number of useful benefits to estate planners, including discounts; control for the donor; avoidance of ancillary probate; and step-up in basis. Whether they will remain viable, however, may depend on whether IRS attacks under Code Section 2703 are sustained in court, and whether Congress makes good on its persistent threats to eliminate the discounts they provide for many businesses. While some practitioners still advocate using them in death-bed situations (on the theory of nothing to

[80] Louis A. Mezzullo, *Family Limited Partnerships and Limited Liability Companies,* 812 *Tax Management Portfolio* (BNA) A-37 (1999).

lose), they should not be attempted without full disclosure of their likely attack at audit and the potential costs of disallowance.

In light of the IRS attacks, estate planners should be circumspect in their recommendation of FLPs. Their first question has to be, is there a bona fide business purpose to the proposed transaction? If the donor's life expectancy is measured in weeks rather than in years, they may be buying their clients an audit in setting these up.[81] The existence of a business purpose, which is the sine qua non of validity, cannot be justified where the donor has been taken off life support – or where the assets are, and will continue to be, personal use property. Merely saving estate taxes does not constitute a valid business purpose, at least as far as the IRS is concerned. While these vehicles are extremely useful where commercial real estate is involved, they become highly questionable where tax avoidance is the only motive for them. And the audit lottery is not particularly helpful where the estate exceeds $1 million.

Once business purpose has been established, the estate planner should seriously consider setting the FLP up in Delaware. Delaware law offers the biggest potential discounts, since its fundamental precept is freedom of contract. Moreover, the limited par5tners are further insulated from liability because of Delaware safe harbors,

[81] See the ages and health of the donors in Tech. Adv. Mem. 98-42-003 (July 2, 1998); 97-19-006 (Jan. 14, 1997); 97-23-009 (Feb. 24, 1997); 97-25-002 (March 3, 1997); 97-30-004; and 97-36-004 (both June 6, 1997).

and there is always the Delaware Court of Chancery if things do not work out.

> If the planner is willing to use a non-Massachusetts entity, he should seriously consider the Delaware LLC as an alternative to the FLP. Not only will it be a simpler entity to manage, but the discounts should be equivalent. Single member LLCs are allowed under Delaware law, whereas they would otherwise be unavailable. In Delaware, unlike Massachusetts, LLCs offer many of the advantages of FLPs, and may reduce their estate tax risks. In light of the black eye that FLPs have recently been given, they may become the only game in town.