

**JOHN CUNNINGHAM'S LLC NEWSLETTER  
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**A BIRD'S-EYE VIEW OF THE LLC WORLD--THE  
16 LLC TYPES**

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EXECUTIVE SUMMARY

LLCs provide legal and tax advantages that no other business organization form can provide. As a result, there are presently about 4 million U.S. LLCs, including about 32,000 LLCs formed under the New Hampshire Limited Liability Company Act and, remarkably, about 360,000 under the Delaware Limited Liability Company Act. These LLCs come in 16 basic types. In understanding the LLC form and in assisting in LLC formations, it is indispensable for both accountants and lawyers to have at least a general familiarity with each of these types and with their various subtypes.

DISCUSSION

- 1) Introduction; the three factors relevant in categorizing LLCs. All LLCs share certain common features—for example, the fact that they may be operated informally and that they provide liability shields to their members. As a result of these common features, the 4 million U.S. LLCs in the aggregate may appear to non-specialists to form a kind of vast amorphous blur.

However, all LLCs can be categorized and assigned to specific LLC types and subtypes on the basis of three relatively simple factors—namely, (i) the number and type of their members; (ii) their management structure; and (iii) their tax structure. On the basis of these three factors, it is possible to identify 16 basic types of LLCs and a total of 41 subtypes. It can be highly beneficial both to accountants and to lawyers to obtain at least a basic understanding of each of these factors. For example, this understanding is indispensable to lawyers in choosing the right model operating agreements for LLCs they are helping clients to form; and it is indispensable to accountants in advising their clients about whether their LLCs have the right management and tax structure. I will briefly address each of these three factors below.

Readers who wish to have comprehensive tables covering the 16 main types of LLCs and the principal subtypes can download these tables by visiting my website at [www.llcformations.com](http://www.llcformations.com) and clicking first on the home page button marked “LLC Library” and then on the link entitled “Overview of LLC Types” (the “LLC Overview”).

- 2) Number and type of members. LLCs can have either a single member or multiple members. Single-member LLCs, in turn, can be separately categorized on the basis of whether their members are individuals or entities. This distinction between individually owned and entity-owned LLCs is important because, among other considerations, the provisions of model operating agreements for the two types of LLCs differ greatly.
- 3) The management structures available to single-member LLCs. As shown in the LLC Overview mentioned above, single-member LLCs owned by individuals can be either member-managed or manager-managed, and manager-managed single-member LLCs owned by individuals can be managed either by the members themselves (called “member-managers” in LLC legal terminology) or by third parties (called “non-member managers”). Single-member LLCs owned by entities can be managed either by a single individual (who can use either the title “manager” or a corporate title such as “president”); by two or more individuals; or by an internal board of directors.
- 4) The management structures available to multi-member LLCs. Whether they are owned by individuals, by entities or by a combination of individuals and entities, multi-member LLCs can have any of three basic management structures—namely, a traditional general partnership structure; a traditional limited partnership structure; or a corporate management structure. However, each of these three structures can be set up either as a simple or as a complex structure.

For example, an LLC that has only a few members and that engages in a group professional practice should generally have a simple general partnership management structure under which each member may participate directly and fully in LLC management and in which there are no management formalities.

By contrast, an LLC that conducts a group professional practice but has many members will generally need a complex management structure that involves committees, annual and special meetings of the members, quorum rules and other specialized governance arrangements needed by larger entities.

- 5) Tax structures available to single-member LLCs. Under the U.S. “Entity Classification” regulations (often referred to by tax professionals and others as the “Check-the-Box Regulations”), single-member LLCs owned by individuals can be subject to federal income taxation as “disregarded entities” (the default federal tax classification), S corporations or C corporations. Most such LLCs should be either disregarded entities or S corporations; only a very few should be C corporations.
- 6) Tax structures available to multi-member LLCs. Under the Check-the-Box Regulations, multi-member LLCs may be taxable as partnerships (the default federal tax classification), C corporations or S corporations. Most such LLCs should be either partnerships or S corporations for federal tax purposes; only a very few should be C corporations. However, it is sometimes useful for LLCs that have corporate management structures to be taxable under Subchapter C. Thus, lawyers should have model operating agreements for this type of LLC as well as for the other types of LLCs mentioned above.

- 7) Two-member LLCs vs. LLCs with three or more members. On the basis of the number of their members, LLC professionals generally think of LLCs as either single-member LLCs or multi-member LLCs. However, from a management viewpoint and for purposes of drafting LLC operating agreements, there are many significant differences between multi-member LLCs with only two members and those with three or more members. Among other things, the issue of management deadlock is ever-present for two-member LLCs but normally far less significant for LLCs with three or more members. This distinction figures significantly in the charts in the above LLC Overview.
- 8) LLCs that are taxable as partnerships tailored to avoid Social Security Taxes and those that are not. In general, individuals who are members of LLCs taxable as partnerships must pay Social Security Taxes on their shares of LLC income unless this income is passive—i.e., income in the form of capital gains, dividends, interest, or real estate rentals. However, a proposed IRS regulation known as Prop. Reg. § 1.1402(a)-2 provides guidelines that enable these individuals to achieve at least a partial avoidance of Social Security Taxes on LLC active income. Thus, in understanding the category of LLCs taxable as partnerships, it is necessary to make a distinction between those that are structured to avoid Social Security Taxes under the Prop. Reg. and those that are not. This distinction, too, is reflected in the LLC Overview mentioned above.
- 9) Series LLCs. In recent years a new type of LLC—namely, the “series” LLC—has emerged. The provisions in LLC statutes that authorize the formation of these LLCs provide, among other things, that the members of a series LLC may hold various classes of assets and various lines of business in various separate “series” and that each such series will be insulated from claims against any other series. Series LLCs thus enable LLC members to avoid the costs and complexities of holding assets and lines of business that they would incur if they held their assets and conducted their various lines of business through multiple LLCs. Instead, each LLC series can be made to function for these members and their LLC like a wholly owned single-member LLC subsidiary. Series LLCs also offer many interesting (but as yet wholly uncharted) possibilities for federal tax avoidance.

However, only five states thus far (namely, Arizona, Delaware, Indiana, Iowa and Oklahoma) have provided for series LLCs in their LLC statutes, and it is doubtful that the above liability protections will be respected by the courts of other states. Thus, the LLC Overview mentioned above makes reference to series LLCs as a separate type of LLC, but this overview calls for only a single basic model operating agreement for them.