

September 20, 2010 | Posted By

[IRS Guidance on Series LLCs](#)

A number of domestic jurisdictions (Delaware, Illinois, Iowa, Nevada, Oklahoma, Tennessee, Texas, Utah and Puerto Rico) have enacted "series LLC" statutes, which provide for the creation of limited liability companies (LLCs) with separate "series." Although such statutes generally do not treat each series as a separate entity for state law purposes, the association of members with one or more particular series is similar to direct ownership in that series, in that the terms of such members' rights, duties, and powers with respect to such series are specifically identified. Series LLC statutes also typically provide that the debts, liabilities and obligations of one series generally are enforceable only against the assets of that series and not against assets of other series or of the series LLC.

Guidance has been lacking as to how such series LLCs should be taxed -- more particularly, whether each series should be treated for tax purposes as a separate taxpayer entity. Although certain states have made a determination (California has stated that generally each series is a separate taxpaying entity and must separately file a state income tax return and pay the annual LLC fee), the IRS has not publicly ruled on the issue.

The IRS has just issued proposed regulations on domestic series LLCs, taking the position that each series of a series LLC must follow the general rules of entity characterization -- that is, if the series has only one associated member, then the default classification generally is to treat the series as a "disregarded entity," but if the series has two or more associated members then the default classification generally is to treat the series as a separate tax partnership. (Of course, a series may also elect to be taxed as a corporation, and in some circumstances may even by default be taxed as a corporation.)

The following is an example provided in the proposed regulations:

Example 1.

(i) Facts. Series LLC is a domestic series organization. Series LLC has three members (1, 2, and 3). Series LLC establishes two series (A and B) pursuant to the LLC statute of state Y. Under general tax principles, Members 1 and 2 are the owners of Series A, and Member 3 is the owner of Series B.

(ii) Analysis. Series A and Series B are each treated as an entity formed under local law. The default classification of Series A is a partnership and of Series B is a disregarded entity. As a result, Series A will be required to file an annual federal partnership return, but Series B will not.

General tax principles would apply to determine who owns an interest in the series and what assets are owned by the series.

The proposed regulations apply similar rules to "protected cell companies," "segregated account companies" and "segregated portfolio companies" that establish multiple accounts, or separate "cells," each of which is identified with a specific participant and each of which is protected from the creditors of any other cell, but which generally is not treated under state law as a legal entity distinct from the cell company. The proposed regulations apply special rules to a foreign series or cell that conducts an insurance business. Entity status of a foreign series that does not conduct an insurance business will be determined by "applicable law" and not by the proposed regulations.

Authored by:

[Matthew Richardson](#)

(213) 617-4222

mrichardson@sheppardmullin.com