

**Life Planning Newsletter**  
**The Law Offices of James A. Busse Jr.**  
**Long Beach CA, Carson City NV.**  
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Planning ..... Asset Protection for the Wary.  
.....Family Limited Partnerships (FLP)

Our law firm focuses on Estate and Life Planning for those who wish to preserve their assets for their family. By doing Probate work for our clients we have established Estate Planning methods that are court tested. Because the goal of every person is to have peace of mind their wishes will be carried out, our integrated approach constantly tests the effectiveness of your Estate Plan with actual California and Nevada Cases. We are particularly involved in Medicaid and Medi-Cal Estate planning. We create Special Needs Trusts and Estate Plans to ensure our clients meet the eligibility requirements, lower their share the cost expense, and reduce or eliminate the potential recovery by the State.

Our law firm integrates low cost Probate with coordinated Estate Planning documents to significantly reduce the impact of the State claim for nursing home care.

This newsletter is provided to our clients free of charge via e-mail and on line at [www.jabusse.com](http://www.jabusse.com)

**Protecting your home from Creditors (FLP's).**

FLP is a slang term. There is no statute that uses Family Limited Partnership, nor does the Internal Revenue Code use it. What "Family Limited Partnership" refers to is a limited partnership formed to hold the family business or investments, with the idea that the parents will make gifts of their limited partnership interests to their children. Since the Parents are often Limited Partners they have some immunity from lawsuits since a Limited Partner's assets are essentially zero. Also, because the limited partnership interests are not liquid, they should be subject to substantial discounts for federal gift and estate tax planning purposes.

Family Limited Partnerships also have some attraction as asset protection vehicles, primarily because the limited partnership interests may be subject to "charging order protection" in some states.

A charging order is an order that allows a person who wins a lawsuit against the partnership to receive the dividends paid to the partners or stockholders of that business first. Of course the savvy FLP general partner stops paying dividends after the judgment and reinvests them in the business. The Charging Order holder, is still assessed the "Business profit" and has to pay the tax on money he or she did not receive (kind of like the reinvested dividends in your mutual fund). Something to think about if you sue a FLP or LLC, or Small Family Corporation. You might win then lose a lot of money because of the charging order.

Unfortunately, FLPs are marketed by numerous promoters who market one-size-fits-all cookie-cutter FLP structures and even sometimes also sell kits allowing clients to engage in do-it-yourself FLP planning. I call this selling a yugo to your ego.

FLPs are almost never correctly utilized. The following brief list is some of the ways creditors and the IRS has BROKEN Family Limited Partnerships and allowed the creditor or IRS to attach the personal assets of the FLP creator. There are more ways:

- Failure to Fund the FLP-** It has to have funds
- Failure to Run the FLP -** It needs to be managed with real records.
- No Business Activities** – There must be a real business reason for the FLP.
- Parent is General Partner** –if the Parent gets sued, the creditor could probably persuade the court to enter an order compelling the Parent to

make a distribution to the Parent's LP interest, totally bypassing the charging order.

**One Person FLP** – The parent owns the whole thing (General and only Limited Partner) so the court says “no protection.”

**One's Living Trust as the GP** Same as above. A living trust equals the individual.

**Formation in the wrong State** – Some States do not limit the creditor's remedy against a limited partnership to a charging order.

**Holding Property in the wrong State** – The state where the assets are may ignore the FLP.

**Failure to Diversify** – All eggs in one basket.

**FLP combined with Foreign Grantor or**

**“Asset Protection” Trust** – This common “Platter” approach is easily recognized and easily broken.

**Fraudulent Transfer** – If you move assets after you know you are going to be sued the court will un-move them.

**Failure to Make Gifts of the LP Interests** – If you don't gift the assets you don't get the tax advantage.

**Failure to Obtain Appraisals** – since the funding of the FLP is evaluated on the date made you must have good records. Your notion of the value is not enough. You need an appraisal.

**Excessive Discount** – Discounts of more than 15% get IRS attention. Discounts of over 20% are mostly sales gimmicks.

**Gifts of Limited Partnership Interests Directly to Children** – Direct gifts are easily attached by creditors or they could kick a SSDI child off the program. Gifting to a trust with Medicaid and spendthrift clauses limits the creditor's ability to get the child's money.

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FLP's have a place in one's estate plan. As with other estate planning, I think it best to partner with a competent attorney or attorney's to properly establish and manage your FLP.

Here are some FLP guidelines; They are not exhaustive.

**Diversify** – It is better to have several smaller FLPs than to have one oversized one.

**Treat the FLP as a Business Entity not a Family Trust** – An FLP is a business, A family Trust is a trust. If the FLP does not have a business purpose, a court will render the FLP a sham and allow the creditor to attach the personal assets without the charging order.

**Have a Good Operating Agreement** -- The agreement should cover what happens when sued.

**Have Trusts Own the Children's LP Interests**  
The children's trust must have spendthrift

clauses and absolute discretion given to the trustee. The Trustee should not be the beneficiary (except maybe in Alaska and Nevada). The trust must not be revocable, and not allow for mandatory distributions for the general welfare (education, health, etc) of the beneficiary.

**Maximize Transfers** – Transfer assets immediately and make annual gifts to children without fail.

**Avoid Kits and Promoters** – If you have enough in assets to justify having an FLP, then you should spend the time to go to an attorney in who has experience in structuring these entities the right way.

**Don't Overuse The Family Limited Partnership (or any other method) The FLP** is just one of many available techniques. Avoid planners who will try to stick nearly everything into the FLP.

The courts are full of people who found out that their FLP didn't protect them. Usually, they found out AFTER they were sued. Some clients have come in after being sued and getting a judgment against them, upset that their “on-Line” FLP didn't protect them. One potential client spent over \$150,000 in legal fees to find out the insurance didn't pay and the FLP didn't work. That person thought he knew what he was doing because he had bought a NOLO book and saw a program on PBS He did his FLP on-Line with a document service started by attorneys so he thought the documents were guaranteed “Iron Clad.” They were only in that the spelling was correct even if out of context “The General Partner will bare the cost...” Of course he didn't read the 150 or so court cases mostly dissolving FLP's. So; the court broke his FLP and the creditor now has a lien on his home.

This newsletter is deliberately a bit vague. The odds are you now know that FLP's are serious business with serious consequences if done and run improperly. They can and do result in significant tax advantages and protection for those who do them correctly, but I don't think many do them correctly on their own.

The next newsletter will review Family Foreign Grantor Trusts as an asset protection strategy.

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