

Three Reasons to Use a Limited Liability Company or Limited Partnership for Real Estate Investments

After searching the market for the perfect piece of real estate, you have found property that will satisfy your needs and give you future opportunities. It is now time to be concerned about protecting yourself from the risks involved in property ownership. One way to reduce such risks is to hold the property through a limited liability entity. By choosing the entity best suited to your specific situation, you will ensure that you have the flexibility and control that you need.

Although other limited liability entities are available, for the following reasons, the preferred entities for real estate investments are the limited liability company (LLC) and the limited partnership (LP):

- **Limited Liability** – As in any business transaction, one of your primary concerns in real estate investment should be your vulnerability. Owning property as an individual or in a general partnership creates unlimited liability. Tenants, guests, and, in some cases, trespassers may sue you for real or imagined grievances. If they prevail, they may seek to use your bank account, home, and personal possessions to satisfy the court's judgment. By using an LLC or LP for real estate investment, you may be able to avoid personal liability for accidents that occur on the property. Liability will be limited to the extent of the LLC's or LP's assets. If anything goes wrong on the property, you will appreciate the protection limited liability provides.
- **Beneficial Management Structure** – Depending upon your specific situation, either an LLC or an LP may provide the management structure you need. An LLC provides a flexible structure that allows members to manage the entity or to elect a manager or a group of managers. All members of an LLC are provided limited liability. Additionally, many states allow one person to form an LLC. On the other hand, LPs require at least one general partner and one limited partner. The general partner is personally liable, but that may be handled by forming a corporation or LLC to serve as general partner, thus encapsulating any liability in a protected entity. When you use an LLC or LP for real estate investment, you may also benefit from estate planning and gifting opportunities available.
- **Reduced Taxation on Appreciated Property** – Although the structure of a corporation may be familiar, corporations are undesirable for real estate investments. If you hold real estate in an LLC or LP and later decide to sell the property to some third party, the tax benefits of using an LLC or LP will become apparent. Unlike a C corporation, LLCs, LPs, and S corporations allow flow-through tax treatment. Profits are only taxed once, while they are taxed twice in a C corporation. Appreciation on the property will result in less tax in an LLC, LP. In addition, an LLC or LP will provide benefits if you transfer the property to your personal use or the personal use of one of your LP partners or LLC members. Such a transfer to personal use would not result in tax consequences. Although other entities may provide limited liability, the tax consequences of using other entities make an LLC or LP preferable.