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## Limited Liability Companies (LLCs) - the Basics for Small Businesses

If you are a small business- one to five people who wish to join to together to run a business- you probably will want to create a Limited Liability Company or LLC. In fact, you may have already done so. It is incredibly easy. All you need to do to create an LLC is to fill out a very simple form( called a Certificate of Formation) and file it with the New Hampshire (or whatever state you wish) Secretary of State, along with a registration fee of \$100.00. You need only state the name of your new company, address, name of registered agent, whether or not it will be managed by a manager or by the members, and the purpose. You also need to answer a couple of questions regarding the sale of membership interests. *Voila!* you have a Limited Liability Company.

### Do You Need A Lawyer to Form an LLC

As you can see from the process above, the basic steps are simple and do not require a lawyer. However, (isn't there always a "however"?) you may want to reconsider that decision, especially if there are two or more of you. I have highlighted some of the issues in the sections below.

### Operating Agreement

An operating agreement is to an LLC what a partnership agreement is to a partnership. The agreement sets out the understanding between the members as to what the company is going to do, the rights and responsibilities of each member, the capital contributions expected of each member, how the company will be managed, voting rights and how profits and losses are to be allocated. it should also detail if, and how, membership interests can be transferred. ***If there is never any misunderstanding or dispute, the operating Agreement will probably never come out of whatever file drawer you put it in.*** That is not reality, however. A well-written agreement will be worth its weight in gold should the day ever come when there is a disagreement and one or more members want out. ***Even if you are the sole member of an LLC you may want to have a well-written operating agreement.***

### What if I do not have an Operating Agreement?

You will have such an agreement. If you do not have one that you approved and signed, you will have one the State of New Hampshire has written for you. The statute enabling LLCs, RSA 304-C, has fifty or more provisions that start with language such as *"Unless a written operating Agreement provides otherwise..."*

One such example is RSA 304-C:110. This section states that unless the operating agreement provides otherwise, a member may not compete with the company. This may be fine for many companies and exactly what you would expect. However, if you have members who are passive investors, they may not want to be restricted in that way. Real estate investors, for example, may want to invest in similar properties that could be construed as competing.

### Oral Operating Agreements

RSA 304-C:40 states *" An operating agreement may be written, oral or implied by a course of dealing or otherwise."* This means that if you have orally agreed to certain practices or even if you have never really discussed how you operate, you may still have an enforceable Operating Agreement. Granted, this may be tough to prove, but a written agreement would go a long way towards disproving it.

### Operating Agreements as "Pre-nuptials"

One of the most overlooked features of an LLC is the potential for disaster upon the breakup of the "marriage" for often an LLC "divorce" is as financially messy as a marriage - and while an LLC dissolution doesn't carry the same potential for emotional trauma as a real marriage, it can be extremely hard on everyone involved. When drafting an Operating Agreement, due thought should be given as to how and under what circumstances a member may withdraw from the LLC.

## Manager Managed or Member Managed?

One of the questions on the Certificate of Formation is whether the LLC will be managed by a manager or by the members. In most cases, small LLCs will probably be managed by the members. Member managed is the simplest form and should be used if the members actually do participate. Manager managed forms are usually used when there are passive investors, although I will sometimes use a Manager managed LLC for estate planning purposes. NOTE: I often see LLCs whose original Certificate of Formation states that it is not managed by a manager but sometime later, the annual reports are submitted using the title "Manager". This is sure to confuse a bank if that LLC is attempting to arrange financing.

## An Operating Agreement as an Estate Planning Tool

Another use of a written operating agreement is as an estate planning tool. A small business may be a very important part of an estate- many times the business is the primary asset. If that asset is tied up in Probate for an extended time, it may devalue quickly. Until someone is appointed Executor, there may be no one to make appropriate decisions. An operating agreement may include a "Transfer on Death" clause that simply transfers a member's interest to his/her beneficiary. Done properly, this may avoid probate. Another way to avoid probate would be to have the membership interest held by the Trustee of a trust, revocable or irrevocable. This, too, would avoid probate. ***These are somewhat sophisticated strategies and although they may be appropriate for even very small companies, they should not be used without counsel from an attorney experienced in both estate planning and LLCs.***

## So Do I Need a Lawyer to Set Up My LLC?

If you can successfully draft an operating agreement that takes all of the above factors- and many more that I do not have time or space to list- into account, then maybe you do not. However, the lack of professional advice could prove to be far more expensive than the fee an attorney would charge. In short, yes, you do need an attorney!

***This is a short overview of some of the issues surrounding LLC formation. It should not be construed as all-encompassing nor as legal advice. This blog cannot create a lawyer-client relationship. Each case is different and LLC formation will be fact specific, that is, what is right for one may not be right for another. Please consult a qualified attorney experienced in these matters.00***

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