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## **Forming a LLC**

### **I. Introduction.**

Your newly chosen LLC begins with a Name Reservation and then the proper filing of your Articles of Organization with the Secretary of State's Office. However, proper planning is highly recommended for the underlying document (the "Operating Agreement") which becomes the governing authority for you and your co-owners within your newly formed LLC.

### **II. Pre-Filing**

Prior to filing the articles, the following issues should be considered.

#### **A. Where should I form the LLC?**

A LLC can be formed in any of the 50 states. In the past, many people have chosen to form a LLC in Delaware because of its history, experience, popularity and pro-business climate. However, your home state of Nevada has also gained popularity due to its pro-business environment and lack of a formal information-sharing agreement with the IRS. Neither Delaware nor Nevada have corporate income taxes, and business filings in these states can usually be performed more quickly than in other states.

Many people also choose to form LLCs in their home state. This may save you money because the LLC will not need to register as a "foreign LLC" if it does business in its home state, and there is no need to pay another person to serve as the registered agent.

If your home state has high annual LLC fees or income taxes, and your LLC does not "do business" in that state, it may be wise to form the LLC elsewhere. "Doing business" means more than just selling products or making passive investments in that state - it usually requires having an office or otherwise having an active business presence.

#### **B. Choosing a Name**

In general, the name of a limited liability company must end with the words "LLC", "L.L.C.", "Limited Liability Company" or "Ltd. Liability Co." The name of a person may be used as part of the name of the limited liability company. Please note that a name will not be accepted if it is likely to mislead the public or if it too closely resembles the name of another LLC formed in that state.

Before you choose the name, you should do a little research to see if the name is taken. THE LAW OFFICES OF KEVIN J. SZOTKOWSKI will conduct a name check for you, or you can search yourself at the Secretary of State of the state in which you wish to form your LLC. Refer to **Names: Section VII** as set forth more fully below for the many restrictions and requirements in selecting your new LLC name.

If the name of the LLC is used in connection with goods or services, you may wish to consider obtaining federal trademark protection for the name. This ensures that no one else in the U.S. may use that name in connection with the same general type of goods or services (except in areas where someone else is already using that name).

### **C. Management by Members or Managers**

A limited liability company may be managed either by (a) the members or (b) one or more managers. A "member" is an owner of the limited liability company. If a limited liability company is managed by the members, then the owners are directly responsible for running the company.

A "manager" is a person elected by the members to manage the limited liability company. In this context, a manager is similar to a director of a corporation, or a member of Congress. A manager can be, but is not required to be, a member. If a limited liability company is managed by managers, then its members are not to be directly responsible for running the company.

Whether a LLC should be managed by members or managers depends on several factors, including:

1. The number of owners;
2. The type of business;
3. Where the owners are located;
4. How involved the members will be in the operations of the LLC.

Management by members is usually the best option for LLCs that have only one member or just a few members, all actively participating in the affairs of the LLC. If there are many members, on the other hand, including some that do not actively participate in the operations of the LLC (such as silent partners), then management by managers may be the best option.

### **D. Officers**

Regardless of how a limited liability company is managed, it can still appoint officers to run the day-to-day operations of the company. A LLC is not, however, required to have officers. Officers serve at the pleasure of either (a) the managers, if the limited liability company is managed by managers, or (b) the members, if the limited liability company is member-managed. Members or managers may both be officers. There is no limit on the maximum number of officers, nor is there a limit on the number of offices that a person may hold. In fact, the same person may hold all offices.

### **E. Registered Agent**

Each LLC must have a registered agent, the person designated to accept official notice if the LLC is "served" with a lawsuit. A registered agent must be either (1) an adult living in the state of formation with a street address (P.O. boxes are not acceptable) or (2) a company (such as THE LAW OFFICES OF KEVIN J. SZOTKOWSKI) registered with the Secretary of State in the state of formation.

As previously mentioned, one of the advantages of forming a LLC in your home state is that any of the members, managers or officers can act as the registered agent. However, there are some advantages to having another person or company act as your registered

agent. First, this adds an extra layer of privacy, since the name and contact information for the registered agent is publicly available. Second, this ensures that if your LLC is named in a lawsuit, no one will surprise you at home on a Sunday night with court papers.

### **III. Capital Contributions and Ownership**

Ownership in a LLC can be expressed in two ways: (1) by percentage; and (2) by membership units, which are similar to shares of stock in a corporation. In either case, ownership confers the right to vote and the right to share in the profits of the LLC.

Unlike a corporation, a LLC can distribute its ownership interests as it pleases, without regard to how much money or property a member contributes to the company. For example, if Owner#1 contributes \$10,000 to the company and is a silent partner, and Owner#2 contributes no money but runs the company on a daily basis, they could still decide to split the membership interests 50%-50%.

A limited liability company can also be organized with different classes of ownership interests, which provides flexibility for special allocations of profits and voting power. For example, you can create a special class of "super-voting" units that provide 10 votes per unit or pay a certain level of profit before the "regular" units.

The sale of membership interests is subject to securities laws. Generally though, if you are not advertising the sale and are dealing only with a small number (less than 35) of knowledgeable and sophisticated investors, then you will be exempt from the regulations. If, however, you are seeking to raise a significant amount of money from a large number of investors, it will be necessary to consult an attorney.

### **IV. Day to Day Operations of a LLC**

#### **A. Separate Affairs**

As previously mentioned, it's important to keep the business and affairs of the LLC separate from a member's or manager's personal affairs. This means setting up a separate bank account, maintaining separate records, and keeping separate accounts.

#### **B. Meetings**

Regular or annual meetings of the members or managers are not required. The operating agreement included with THE LAW OFFICES OF KEVIN J. SZOTKOWSKI LLC formation package does not require regular meetings, but states that meetings may be held as the members or managers deem them necessary to run the company. Even though it's not required by law, it may be a good idea to keep records of the actions taken or approved at the meetings.

#### **C. Assignment and transfer of ownership interests**

Transfer of membership interests generally requires the consent of other members. However, THE LAW OFFICES OF KEVIN J. SZOTKOWSKI allows you to change the default rule if you desire. This is an important issue to consider for any LLC with more than one member. On one hand, you may wish to sell or transfer your membership units to anyone you wish. On the other, if you consider the other members of the LLC your business partners, you may want approval over whether they can transfer their interest and who they can transfer it to.

## **D. Tax forms and licenses**

Many LLCs are required to obtain a federal tax identification number, which is similar to an individual's social security number. However, there are some situations where a LLC can simply use the social security number of the owner. City and county business licenses may also be required. Please check with an accountant about the need for a tax ID number and your city and county to see which types of licenses are needed.

## **V. Tax Reporting**

Although LLCs do not pay federal taxes, they must still prepare a separate tax return each year and file it with the IRS. The LLC's income is passed through to the members, who must recognize their allocated income or loss on their personal tax returns.

If a LLC elects to be taxed as a partnership and its fiscal year ends on December 31, the tax return is due April 15. The LLC must file a tax return on Form 1065 even if it does not have income or no tax is due.

A LLC with employees is required to pay federal (and sometimes state) payroll taxes. Furthermore, some states, including California, have an annual LLC fee that is based loosely on the company's net income.

## **VI. State Requirements**

The formation of a LLC (limited liability company), and the ongoing obligations for that LLC, will vary somewhat from state to state. While the process may seem similar for forming a LLC in Nevada and California, for example, there could be small differences in formation requirements that might not be immediately evident.

Fortunately, when you form your LLC with THE LAW OFFICES OF KEVIN J. SZOTKOWSKI, we make sure your legal documents conform with the specific state requirements where you form your LLC. However, you'll want to be aware of the specific ongoing obligations that the state requires for your LLC. Typically, you can go to the Secretary of State website for the state in which you've formed your LLC for all of this information and more.

## **VII. Names**

**Registering a Limited Liability Company Name:** Choosing a business name is one of the first steps in the process of forming your Nevada Limited Liability Company. The name that you choose:

1. Must contain, as the last words of the name, "Limited-Liability Company," "Limited Liability Company," "Limited Company," or "Limited" or the abbreviations "Ltd.," "L.L.C.," "L.C.," "LLC" or "LC." The word "Company" may be abbreviated as "Co."
2. Must be distinguishable from (cannot be the same as or deceptively similar to): from the names of any other Nevada Limited Liability Company and all other artificial persons formed, organized, registered or qualified that are on file in the Office of the Secretary of State and all names that are reserved in the Office of the Secretary of State.
3. May be the name of a LLC whose charter has been revoked, which has merged and is not the surviving entity or whose existence has otherwise terminated.
4. Must not contain the word "accountant," "accounting," "accountancy," "auditor" or "auditing" unless the Nevada State Board of Accountancy certifies that the limited-liability company:
5. Is registered pursuant to the provisions of chapter 628 of NRS.

6. Has filed with the Nevada State Board of Accountancy under penalty of perjury a written statement that the LLC is not engaged in the practice of accounting and is not offering to practice accounting in this state.
7. Must not contain the word "bank" or "trust" unless:
  - a. It appears from the articles or an amendment that the LLC proposes to carry on business as a banking or trust company, exclusively or in connection with its business as a bank, savings and loan association or thrift company; and
  - b. The articles or certificate of amendment is first approved by the Commissioner of Financial Institutions.
8. Must not contain the words "engineer," "engineered," "engineering," "professional engineer," "registered engineer" or "licensed engineer" unless:
  - a. The State Board of Professional Engineers and Land Surveyors certifies that the principals of the limited-liability company are licensed to practice engineering pursuant to the laws of this state OR
  - b. The State Board of Professional Engineers and Land Surveyors certifies that the limited-liability company is exempt from any prohibitions.

THE LAW OFFICES OF KEVIN J. SZOTKOWSKI allows you to choose up to 3 names, in order of preference. We will conduct a name check for your Nevada Limited Liability Company before filing to see which names are available.

**Registering a Limited Liability Company Name:** Once you have chosen an available name, THE LAW OFFICES OF KEVIN J. SZOTKOWSKI can help you register your name with the state.

## **VIII. Formation Requirements**

**A. Articles of Organization:** In any Nevada LLC formation, articles of organization must be signed by at least two persons organizing the LLC and delivered, along with a copy, to the Nevada Secretary of State, Corporations Division for filing. State law requires that certain information be included in your articles of organization for your Nevada LLC formation. This information must include:

1. The LLC **name**;
2. The name and complete street address of its **resident agent**, and the mailing address of the resident agent if different from the street address;
3. The name and address, either residence or business, of each of the organizers signing the articles;
4. If the company is to be managed by: (1) One or more **managers**, the name and address, either residence or business, of each initial manager; or (2) The members, the name and address, either residence or business, of each initial member;
5. Any other provisions, not inconsistent with law, for the regulation of the internal affairs of the LLC, including any provisions which under this chapter are required or permitted to be set out in the operating agreement of the company.

**B. Filing:** Your LLC is considered organized once the original articles of organization and one (1) exact or conformed copy is delivered to the Corporations Division of the Secretary of State by one or more persons and signed by one or more organizers.

A certificate of organization will be issued and delivered along with the conformed copy to the representative of the LLC. The original articles of organization will in turn be filed with the Secretary of State along with the month, day and year of filing.

**C. Operating Agreement:** Although not required, LLC members may adopt an operating agreement to regulate the internal affairs of the company, including the management of the LLC, which may also be amended and repealed as allowed by the agreement or applicable law.

**D. Membership:** A LLC must have at least one or more members. Requirements:

1. Minimum Number of Members: One or more;
2. Eligibility Requirements:
3. Procedure for Membership:

**E. Resignation of Membership:** Certain prohibitions exist surrounding the ability of a member to resign from the company.

A member may not resign from a limited liability company except in accordance with the operating agreement.

If the resignation or withdrawal of a member violates the operating agreement:

- a. The amount payable to the member who has resigned or withdrawn is the fair market value of his interest reduced by the amount of all damages sustained by the company or its other members as a result of the violation; and
- b. The company may defer the payment for so long as necessary to prevent unreasonable hardship to the company.

A member who resigns or withdraws ceases to be a member, has no voting rights and has no right to participate in the management of the company, even if under this section a payment due him from the company is deferred.

**F. Contribution:** The contributions of a member to the LLC may consist of cash, property or services rendered, or a promissory note or other binding obligation to contribute cash or property or to perform services

**G. Registered Office:** The registered office may be but does not need to be the LLC's place of business. Each LLC must designate a street address for the service of process.

## **H. Taxes and Fees**

Once a Nevada LLC has been created, the Nevada Secretary of State will require certain recurring responsibilities and duties. The most important of these are explained below. For further information, refer to the Nevada Secretary of State.

## **I. Continuing Obligations**

**Records:** Each limited liability company shall keep following records open to inspection at its office:

1. A current list of the full name and last known business address of each member and manager, separately identifying the members in alphabetical order and the managers, if any, in alphabetical order;
2. A copy of the filed articles of organization and all amendments thereto or restatements thereof;
3. Executed copies of any powers of attorney pursuant to which any certificate or amendment was executed;
4. A copy of any then effective operating agreement

## **IX. Dissolution**

**Acts Triggering Dissolution:** A LLC is dissolved upon the happening of any one of the following events:

1. Expiration of the duration of the LLC specified in the articles or operating agreement;
2. Occurrence of event specified in writing in the operating agreement;
3. Upon the affirmative vote or written agreement of all members unless otherwise provided in the articles or operating agreement;
4. Upon entry of a court order

## **X. Taxes**

A LLC can offer certain tax advantages over a corporation, including the availability of more deductions. Additionally, a LLC is not required to be a separate tax entity like a corporation; instead it can be a “pass-through entity” so that the LLC owners report business losses or profits on their personal tax returns, like a partnership.

**Federal Income Tax:** Unless you elect to tax the LLC as a corporation, the IRS treats single-member LLCs as sole proprietorships for tax purposes. This means the LLC itself does not pay taxes and does not have to file a tax return. Unless you elect to tax the limited liability company as a corporation, the IRS treats multi-owned LLCs as partnerships for tax purposes. This means that LLC owners each pay taxes on their lawful share of the profits on their personal income tax returns, not the LLC itself. If you desire, by filing IRS Form 8832, you may elect corporate taxation if you regularly need to keep a substantial amount of profits in your LLC.

**Federal Tax Identification Number:** Your LLC may need to obtain a federal tax identification number (also known as an employment identification number/ EIN), which is similar to an individual’s social security number. Generally, you will not need a separate EIN number for your LLC as long as you are the sole owner and the LLC has no employees. However, if you are not the sole owner of the LLC or if the LLC has employees, your LLC will need a separate EIN number to open a bank account and for certain tax filing requirements. THE LAW OFFICES OF KEVIN J. SZOTKOWSKI can prepare your Federal Tax ID Application if you have not already done so.