

Practical Tips for Business Owners on When and How to Form an LLC



Operating your business through properly formed and managed entities, such as a corporation or a limited liability company (an “LLC”), is one of the most effective ways to limit your personal liability for the obligations and legal liabilities of your business. All states now allow the formation of LLCs for annual fees varying from \$300 to \$1,000. They’ve quickly surpassed corporations and limited partnerships as the most common type of new entity formed for small businesses. Their flexible simple management and operations structure make them an ideal fit for businesses that do not require the complicated management structures of a Corporation or the strict limitations of a Limited Partnership.

The specific protections and advantages of an LLC vary somewhat by state, but are generally similar. There is no requirement that an LLC be formed in the state where the business operates or is has its main office. For example, you can buy a Manufactured Home Community in Oklahoma, live in California, and form the park owning LLC in Nevada. But if you do create your LLC in the state where your park or business is located, you won’t have to register in that state as a foreign entity and hire a third party to accept service of legal documents there. This saves money over the long run.



While an LLC may have officers like a corporation (ex. President, V.P., Secretary...), they aren't required. Statutorily, an LLC is managed by either its Members (the owners of the LLC) or by its Managers (persons elected by the owners to manage the LLC). Managers can be Members themselves or a third party who has no ownership at all in the LLC. Most state LLC formation statues regarding the operations and structure of an LLC are intentionally flexible regarding management. When signing documents, an LLC Manager can sign as "Manager," "Member," or even under a formal corporate title such as "President" or "Treasurer," if such titles are included on your LLC records.

When you file to form an LLC with a state's Secretary of State, the application will ask if you want to be "Member" managed or "Manager" managed. I generally recommend the "Manager" managed option because:



- a) There's more anonymity regarding the actual ownership of the LLC when forming the entity and filing annual tax reports. In a Manager-managed LLC, only the Managers (not the members/owners) are listed on the Certificate of Formation;
- b) There's more flexibility regarding transfers of ownership. Owners are not named in the formation and annual reporting of the LLC and changes in ownership are not reported; and
- c) There remains the ability to name nonmembers as Managers of the LLC. Since a Manager does not have to be an owner of the LLC, having the entity be Manager-managed gives the LLC the flexibility of hiring a non-owner third party to serve as the manager of the entity.



The most expensive part of forming an LLC or Corporation is often the creation of an Operating Agreement, which is normally written by a lawyer and cost \$1,500 or more. Operating Agreements set forth the formal rules regarding ownership and management of the entity and are usually 40 to 100 pages long. These are needed and valuable documents if you have multiple owners or investors. However, if the only owner is you and or a spouse, the value of such a document drops significantly because you're

not likely to have a big dispute with yourself. Operating Agreements are not required.

To form your LLC, file a Certificate of Formation with the Secretary of State in the state where you want to form your LLC. The Certificate of Formation is generally only five or six questions long. In most cases, you'll want the duration of your business to be listed as perpetual and list the Purpose of the business as "Any and all lawful purposes." Generally speaking it's also useful to acquire an Employer Identification Number or EIN, also known as a Federal Tax identification number, from the IRS yourself promptly and easily by visiting the IRS website (www.irs.gov). EIN's are often required by banks when you open an account in your new LLC's name, plus they are handy for tax purposes. Of course, as with any decision regarding the formation and operations of an entity, it is valuable to visit with your CPA or lawyer about what's best for you.

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