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**SMALL BUSINESS**

# Everything You Need to Know About LLCs to Help Your Clients

Popular for its owner liability protections and flexible tax options, the Limited Liability Company (LLC) is a legal structure option worth exploring for clients who are starting or growing businesses.

**Nellie Akalp** • Jun. 23, 2021



Popular for its owner liability protections and flexible tax options, the **Limited Liability Company (LLC)** is a legal structure option worth exploring for clients who are starting or growing businesses.

In essence, the LLC is a hybrid of a partnership and a corporation. Like the corporation, the main benefit is, as the name implies, the owners have limited liability. An added advantage is profits may be taxed like a partnership/sole proprietorship, which passes through to the owners (members), avoiding the “double taxation” corporations face.

Unlike corporations, which can exist indefinitely (if corporate compliance is met), most states limit the lifespan of LLCs to 30 years before requiring renewal. To raise money, LLCs can offer percentages of ownership and rewrite the operating agreement to reflect the change.

LLC company owners are called members, and although the compliance requirements for LLCs are more relaxed than for corporations, there are still some questions your clients may have on member guidelines. Here’s what you need to know about LLC member guidelines, including the difference between single vs. multi-member LLCs, member-managed vs. manager-managed LLCs, how to add new LLC members, LLC membership interests, and more.

## **Steps to Starting an LLC**

As with a corporation, the steps to starting an LLC begin at the Secretary of State’s office:

- 1. Name search.** Searching the state’s database ensures the chosen name of the LLC is not already in use. If the name is clear, the owner must register it with the state. Some states require the initials “LLC” to appear at the end of the name.
- 2. Articles of Organization.** The Articles of Organization is a legal document filed with the state containing critical information about the company such as the legal name, management type, date of formation, names, and information about the members and their obligations. Once the Secretary of State approves the document, the LLC is recognized as a separate legal entity, and that state is considered the LLC’s home state.
- 3. Acquire a Federal Tax ID number or EIN.** A Tax ID or EIN (Employer Identification Number) is a nine-digit unique number provided by the Internal Revenue Service to identify a business. The business must have a Tax ID number or EIN to open a business bank account, hire employees, file for licenses and permits,

and pursue other business activities.

**4. Create an Operating Agreement.** The LLC Operating Agreement officially documents the internal organization of the company—the roles and duties of its members and managers. Although not all states require LLCs to have an Operating Agreement, it's recommended to have one because it outlines the LLC's financial and practical decisions. Once agreed upon and signed by all members, the document further protects the owners from personal liability. In addition, the Operating Agreement specifies how business agreements and disagreements are solved and how members may be added or removed.

Once established, the LLC must also adhere to the continuing compliance requirements to remain in good standing with the state. The LLC must file annual reports, hold member meetings, and update the state about any changes to the business, such as a change of address and membership.

## **The Difference Between Single Vs. Multi-Member LLCs**

As the term suggests, a single-member LLC has only one owner (member). If there are two or more members, it is considered a multi-member LLC. The single-member LLC has complete control over the company, and the LLC is its legal entity, separate from its owner. In a multi-member LLC, the members share ownership, but the business is legally independent of the owners. Multi-member LLCs can have an unlimited number of members (unless it elects to file taxes as an S Corp, which allows for only 100 or fewer members).

For income tax purposes, the single-member LLC is deemed a “disregarded entity” by the Internal Revenue Service, and its profits and losses are reflected on the owner's federal tax return. The single-member LLC may elect to be taxed as a corporation.

Multi-member LLCs are taxed as partnerships with the profits and losses divided evenly among the members unless otherwise specified in the LLC's Operating Agreement. Percentages of ownership are typically called “LLC units.” Multi-member LLCs can also file as a C Corp or S Corp if they so choose.

## **The Difference Between Member-Managed and Manager-Managed LLCs**

The single-member LLC is also considered the manager. In a multi-member LLC, the members must stipulate whether the LLC will be member-managed or manager-managed.

In a member-managed LLC, all the members agree to participate in the operation and decisions of the company. The majority of owners must agree when making important company decisions, including signing contracts and applying for loans. If an LLC does not stipulate otherwise, the state considers the LLC member-managed by default.

A multi-member LLC can alternately choose to appoint a manager (or managers) to run the LLC. In a manager-managed LLC, one or several members can be in charge of daily operations and making company decisions. Other members of the LLC can participate or have a passive role.

The management type and names of the managers should be outlined in the Articles of Organization. Document any specific responsibilities in the LLC's Operating Agreement.

## **How to Add New LLC Members**

While adding new members is not a difficult task, your client should consider all the ramifications involved. For instance, a new member/s could mean a new source of working capital and/or additional strategic expertise. However, the percentage of ownership of all current members is reduced, and it may be harder to make company decisions with more voices wanting to be heard. Before adding new members, advise your client to think through all possible advantages and consequences.

Next, the LLC members need to review the previously agreed-upon procedure in the Operating Agreement for adding members and check to see if there are additional state guidelines. Following a written process proves the company operates as its own entity. The terms of the ownership structure dictate what rights and duties the new member takes on. Make sure your client documents their decisions.

Finally, all members are required to vote to add a new member/s and sign any amendment made to the Articles of Organization/Operating Agreement. The amendments then get filed with the state

States don't put many restrictions on who can be a member of an LLC. Members must be over 18 years old and do not have to be U.S. citizens. Members don't even have to be a person—other entities, such as corporations, S Corps, LLCs, and trusts, can be members.

## **How LLCs Can Raise Money**

An LLC can raise money by offering members a percentage of ownership interest or LLC membership units. Members with interests have a stake in the profits of the LLC and typically have a voting interest. LLCs are not restricted in distributing membership, and the amount of monetary investment does not have to equal the amount of interest the member receives. Member interests can also be transferred or sold.

Your client needs to comply with the agreed-upon rules for dispersing member interests outlined in the LLC Operating Agreement. Member interests should be consistently summarized as percentages or units. What will be accepted for member interests should also be specified (for example, can a member receive interest only in exchange for cash, or are member services acceptable?).

Lastly, the LLC must keep all documentation and maintain good records about member interests in the Operating Agreement. Membership certificates, transfers of interests (called Membership Interest Assignments), and member interest balance sheets are vital records to keep on hand in case the LLC's activities are ever called into question.

The LLC is a flexible and beneficial [legal structure](#) your clients should consider when starting or taking their businesses to the next level. The more you know about LLC member guidelines, the better you can steer them to make informed decisions.

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*Nellie Akalp is a passionate entrepreneur, business expert, and mother of four. She is the CEO of [CorpNet.com](#), a trusted resource and service provider for business incorporation, LLC filings, and corporate compliance services in all 50 states. Nellie and her team recently launched a partner program for accountants, lawyers, and business professionals to help them streamline the business incorporation and compliance process for their clients.*

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