



## TIPS FOR ENTREPRENEURS



# Limited Liability Company (LLC)

## What Is a Limited Liability Company?

Businesses usually form a Limited Liability Company (LLC) to limit members' personal liability. The LLC is distinct from its members, so its debts, obligations, or other liabilities are solely the LLC's responsibility. With a few exceptions, members or managers are not directly or indirectly liable. An LLC is a pass-through entity, meaning it receives all income and distributes it to LLC members for tax purposes. The duration of an LLC can be for a set period or perpetual.

## Forming a Limited Liability Company (LLC)

To form an LLC, complete a Certificate of Organization through Idaho's secretary of state office (found online at <https://sosbiz.idaho.gov/auth?page=login>). On this website, submit contact information for all LLC members and indicate if an agent will represent the organization. If the LLC is a professional entity, describe the type of professional services it will offer and ensure that its members are fully licensed. Before you begin, though, be sure your business name is not already used by another business by searching at <https://sosbiz.idaho.gov/search/business>. The recent expense for filing an LLC with the Idaho secretary of the state's office is a one-time fee of only USD \$100 or USD \$120 for submitting a paper form.

## Register an LLC with the Federal Government

Once you have registered your LLC with the state of Idaho, you may also need to register it with the federal government, especially if your type of business requires an Employer Identification Number (EIN). You need an EIN if you

- Have or plan to hire employees.
- Plan on filing employment, excise, or Alcohol, Tobacco, and Firearms taxes.
- Withhold taxes on income, other than wages, paid to a nonresident alien.
- Have a Keogh plan.
- Are involved with any of the following organizations: trusts (except certain grantor-owned revocable trusts,

individual retirement accounts [IRAs], and Exempt Organization Business Income Tax Returns [Internal Revenue Service (IRS) Form 990-T]), estates, real estate mortgage investment conduits, nonprofit organizations, farmers' cooperatives, and plan administrators.

- Want to apply for government contracts.
- Want to file for trademark protection with the United States Patent and Trademark Office.

To register your LLC with the federal government, you need to apply for an EIN using IRS Form SS-4. Also, you can apply online at <https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online>.

**PLEASE NOTE: This handout does not offer or substitute for legal advice. For more information: CALS-RuralStudies@uidaho.edu.**

## Keeping Your Limited Liability

Your liability protection, as a member of an LLC, does not protect you from wrongdoing or personal guarantees you may extend on which your LLC defaults. To enjoy limited personal liability, be sure to

- Have a separate bank account for managing your LLC funds to ensure they do not commingle with your personal expenses. Keep your personal finances out of your LLC accounting books.
- Have an operating agreement and ensure that the proper documentation is filed with the state or federal government, reflecting the authenticity of the members as active agents of the LLC.
- Reflect the status of your LLC on your business signs and letterheads.

## Contents of an Operating Agreement

An LLC needs an operating agreement that provides members with information about their rights, duties, and obligations. This agreement should include the following information:

- Policies related to day-to-day operations
- How many and what positions will be created
- Whether the LLC will be managed by LLC members or by managers with no membership or interest in the LLC
- How voting will take place
- Fiduciary<sup>1</sup> duties and duties of loyalty the LLC owes to its members and the public
- How to handle major changes in the company's operations and resolve conflicts that may arise
- What constitutes a violation of the terms or policies of the operating agreement and how to handle it
- Members' rights to exit the LLC
- How to dissolve the company
- Multiple-member LLCs should add "safe harbor" provisions in their agreements to ensure proper allocations of profit and loss per the Internal Revenue Code (IRC). See Treasury Regulation Section 1.704-1(b).

## How the LLC and Its Members Interact with Others

The LLC can deliver a statement to the secretary of state that explains the positions created within the LLC to prevent any misunderstanding or undue liability and to establish limitations of actors binding the LLC. This statement describes each position's respective authority to execute transactions, contracts, etc. and a time frame for that authority to exist.

Note that a member of the LLC is not necessarily an agent of the LLC; however, a person or manager acting on behalf of the LLC could be considered an agent. An LLC member who does not act as an agent or on behalf of the LLC does not have complete protection from liability, even though the LLC itself has limited liability. In some cases, it may be necessary to inform the secretary of state that the LLC denies responsibility for specific actions taken by actors who did not have the authority to act on the LLC's behalf or to inform the state of the termination of an actor's authority.

## LLC Membership

An LLC can be formed by one person who becomes a member and organizer at the same time. If there are multiple members, one member can be appointed as the organizer who can act on behalf of the company. An organizer does not have to be a member and can be anyone appointed by the members. After formation, additional members can be added by a majority vote of current members.

Members can contribute to the LLC, including property transferred into the LLC, services performed, or another benefit provided to the LLC or agreed to be transferred in the future. The agreement must be fulfilled regardless of death, disability, termination, or any other member's inabilities. If the LLC dissolves, members have rights to distributions, except when a member dissociates from the LLC contrary to the agreement.

<sup>1</sup> A fiduciary is a person or legal entity that has the power and responsibility of acting for another (usually called the beneficiary or principal) in situations requiring total trust, good faith, and honesty.

## Interests in the LLC

An interest in the LLC can take many forms, including money invested, property transferred, services performed, etc. If an LLC member dies, a legal representative may exercise the deceased member's rights, responsibilities, and/or liabilities.

A member can transfer their interest outside the LLC without considering a dissociation<sup>2</sup> from the LLC. The party receiving the transferred interest is not entitled to participate in the LLC's management. Still, it may have other rights, such as access to records, information about LLC management, or receipt of distributions. The party must offer to the LLC proof of ownership of such interest.

The transference of interest may have requirements necessary to be fulfilled before the transference becomes effective; otherwise, the transference is deemed ineffective.

## Dissociation from an LLC

A member of an existing LLC can voluntarily opt for dissociation from the LLC. It is also possible to expel a member from the LLC involuntarily by having a majority of other members cast a vote to expel a member. A member can withdraw from the LLC at any time using their right to dissociation.

## LLC and Income Taxes

As mentioned previously, an LLC is a pass-through entity, so the business income passes to its members for tax purposes. However, an LLC may elect to be treated as a corporation for tax purposes using IRS Form 8832.

If the LLC has only one member, the IRS treats the LLC as sole proprietorship for tax purposes. Report your business's income and expenses on your individual tax returns using IRS Form 1040 Schedule C. Also, your LLC can be treated as a sole proprietorship for tax purposes if your only partner in the LLC is your spouse.

If your LLC has more than one member, each owner pays taxes on their share of the profits on their personal income tax using IRS Form 1040 Schedule E and 1065.

We recommend asking a tax professional or qualified tax attorney for advice and visiting the IRS website for more information.

## Additional Resources

Idaho Code Title 30 Chapter 25 provides the basic rules for limited liability companies:

<https://legislature.idaho.gov/statutesrules/idstat/Title30/T30CH25/>

NOLO: <https://www.nolo.com/legal-encyclopedia/idaho-form-llc-32194.html>

Northwest Registered Agent: <https://www.northwestregisteredagent.com/llc/idaho>

TRUiC (free guide): <https://howtostartanllc.com/idaho-llc#to-start>

<sup>2</sup> Dissociation of a member happens when a person is expelled as a member or the person's express will to withdraw as a member. For more information see section 30-25-602, Events Causing Dissociation-Idaho State Legislature.

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