



Single Member LLCs

Do you need an Operating Agreement?



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Introduction – Often one or more people create a limited liability company (LLC) when starting an enterprise in order to protect personal assets, promote growth and gain credibility. In many cases the LLC has multiple members. In other situations, however, a person may create a single-member LLC in which the person starting the business, buying an investment property, etc., is the only member.

For multi-member LLCs, the members typically create an operating agreement. Among other things, an operating agreement lists the duties of the members, their ownership interests, how decisions are made, their rights and responsibilities, and exit strategies. It is similar to a partnership agreement or shareholder's agreement.

When a person (or a business) creates an LLC that has only a single member, they may wonder if having an operating agreement provides any benefits. Some key reasons for a single-member LLC to have an operating agreement are discussed below.

- **Personal Liability Protection** – One of the benefits of an LLC is to protect the member's personal assets, such as a home or financial accounts, from lawsuits that arise from the business of the LLC. An operating agreement demonstrates that the LLC is a real business and is separate entity from the owner by documenting the structure of the LLC. Without an operating agreement, the business may appear more like a sole proprietorship which does not limit the member's financial liability.





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- **Personal Liability Protection (cont.)** – In extreme cases, a court may not recognize the LLC as a separate entity from the owner, and consequently will not permit the liability protection advantages that an LLC offers.
- **State Default Rules** – Without an operating agreement, the LLC is bound by the default laws of the state in which it was formed. For example, the member may want to designate a specific individual to take over the LLC in case of death or injury. Without this being stated in the operating agreement, the laws of the state would apply instead of what the member wants.
- **Required by others** – When the person who created the business seeks financing for their LLC, the lender may require an operating agreement as proof that the individual owns the LLC. Registration with the state may not suffice to demonstrate ownership. If other investors are being brought in to the entity, those investors may require an operating agreement to understand how the business operates, is structured and their ownership interests. Some professional organization, such as realtors, may require their members to provide an operating agreement for their LLC.
- **Manager** – A business owner may want to bring in a business manager, at some point, to operate the business. The operating agreement is an excellent way to define the manager's powers and the manager's compensation.

Conclusions – Even for a single member LLC, a well written operating agreement provides multiple benefits. An experienced business attorney can help draft an operating agreement to take advantage of all the benefits discussed in this article.

