7 Topics To Address In Every LLC Operating Agreement

Description

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Too many closely-held businesses suffer from poorly drafted operating or shareholder agreements, or have no written agreements in place at all. Without good documentation, there is no road map to guide the partners when the going gets tough. And, when the going gets tough, the tough often hire lawyers. The first thing a good lawyer will do is review the operating documents, if they exist.

Whether you are an LLC with an operating agreement, a corporation with a shareholdersâ€™ agreement, or a general partnership with a partnership agreement, your written agreement should cover the 7-Ds: Death, Disability, Disagreement, Disharmony, Departure, Divorce and Dissolution.

If a partner dies or becomes permanently disabled, the agreement should include a procedure for valuing and buying out the partnerâ€™s interest. The buyout is often covered by life or disability buyout insurance, or through a payment plan if no insurance is available.

Disagreements typically relate to major matters affecting the business as a whole, whereas disharmony deals with partner behavior and the relationship between or among partners. For example, whether or not to open for business on Sunday is a disagreement, but your partnerâ€™s failure to consistently show up for work on time creates disharmony. Your agreement should provide for a clear process to address disagreements and to resolve issues leading to disharmony.

Departure may be amicable or non-amicable, depending on the circumstances. A thoughtfully prepared agreement will address both kinds of departures to ensure that in the event of a partner transition, the business is not adversely affected.

Dissolution of the business entity could be due to failure, or as the result of a change of circumstances, such as a sale. Provisions providing for an orderly wind down or transition of the business should be included in any agreement.

In the event of a partnerâ€™s divorce from his or her spouse, the remaining partner(s) will want to avoid having the spouse step into any active role in the partnership. Without an agreement in place to address this situation, it may be difficult to keep a former spouse out of the business entirely.

The risks associated with failing to enter into a written agreement for the operation of the business can vary depending on the state of formation and the type of business entity. For instance, under Delaware law, the term â€œlimited liability company agreementâ€• is defined as â€œany agreement . . .Â**written, oral or implied**, of the member or members as to the affairs of a limited liability company and the conduct of its business.â€• (emphasis added). Thus, if members of a Delaware LLC fail to enter into a written agreement, they leave open the possibility for a court to find that there was an oral or implied agreement. The members could find themselves bound by terms that one or more of the business owners would not have agreed to in a written agreement.

Do you want to have a strong written agreement in place for you and your partners? ContactÂ Colin Coleman Â orÂ Brian ReillyÂ to discuss how we can help you.

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