



TOP 5%
CLUB

Corporate and LLC Formalities

*With Sherwood Cook, Attorney and One of Nevada's "Legal Elite" -
According to Nevada Business Magazine*

Be Successful and Run Your Business Right with these Corporate and LLC Formalities...Made Simple:

- *What are corporate and LLC formalities - and why are they important?*
- *What are the requirements of a one-person corporation or a one-person, single member, LLC?*
- *What's the difference in an LLC being managed by managers or managed by members?*
- *What should you be documenting in your LLC or corporation?*
- *How do you amend the name of a corporation?*
- *How do you go back and update records?*
- *What are the steps to dissolving a corporation or an LLC?*



**Build Your Profits Fast...
And Protect Them!**

Sherwood Cook

Top 5% Interview

Scott: Well, good afternoon, everyone. This is Scott Letourneau, the CEO of Nevada Corporate Planners and Fast Business Credit. Welcome to another one of our Top 5% Club Monthly Teleseminars, where our goal is to help your business be part of the top 5% that not only succeeds and is profitable after 5 years, but that helps you beat the odds of business failure rate.

In order to be part of the top 5%, you've really got to master 2 skills: 1) how to grow your profits in the shortest period of time possible; 2) how to keep them. How to keep them involves many areas, as far as structure, protecting your assets, and making sure you're operating your separate legal entity, whether an LLC or a corporation, in a proper format, and doing the formalities that are required so you can maintain that protection, so you can separate your personal and business liabilities as best possible.

Today, we're going to talk about a very important subject: corporate and LLC formalities made simple. A lot of people I know out there, when you formed an LLC or corporation, when you filled out the record book, we went through all the initial formalities and filled it out. Maybe we hear from you on an annual basis. But in between, sometimes the ball gets dropped a little bit. You may have been making some decisions that require some formalities to be updated throughout the year; because, after all, the corporation LLC is the separate legal entity from you. It can pretty much do everything you can do except act and think, and it does that through paperwork: minutes, meetings, resolutions, things of that nature.

It's very, very important to make sure you run it as a separate legal entity. Because if your entity eventually gets sued, and if you didn't

run it or operate it properly, there is the possibility of what's called "piercing the entity," corporate, or LLC veil," which means then they go after you personally.

Even though Nevada has a better level of protection in this area in general, we still recommend, strongly, you do all these formalities properly, so you can be assured that if you're checked on by a legal issue, or even if the IRS comes at you and says, "Was that authorized to take that business trip?" that you have those proper minutes and meetings and resolutions in place. Even for LLC's, this is critical.

What I've done to kind of simplify the process and explain the basic fundamentals and go into a couple situations, especially if you are in a partnership with an outside partner, it's critical, even if owners come and go or officers and directors come and go.

I've invited a very sharp guy in this area. He's an attorney here in Nevada. His name is Sherwood Cook.

He's a shareholder of Durham Jones & Pinegar, in the firm's Corporate and Securities section. His practice covers a wide variety of business-related transactions and compliance areas of law, including business formation, planning, capital-raising alternatives, debt and equity security offerings, security law compliance.

Mr. Cook's practice also includes personal estate planning and business succession planning, both very important subjects.

From 1987 to 1990, Mr. Cook served as the Nevada Deputy Secretary of State for Securities. So, when it comes to raising money and the issues, if you're looking for investors, we won't cover that in this call per se, but definitely Sherwood Cook is the guy you want to talk to in this area.

In 2009, Mr. Cook was recognized by *Nevada Business* magazine as one of Nevada's "Legal Elite" among the state's top 100 attorneys.

I'd like to welcome to the call our special guest, Sherwood Cook.
Sherwood, how are you doing today?

Sherwood: I'm doing well, Scott. Thank you for having me.

Scott: Yeah, it's a pleasure to have you on the call. This is such an important subject, and I think one that's overlooked because, as you know, Sherwood, when people start their businesses, it's almost like they can't wait to get all these formalities and legal stuff out of the way so they can go off and start making money. And, off and running they go.

Sometimes – let's be honest, most of the time – they forget to revisit formalities throughout the year and on an annual basis.

Of course, everything goes well until you have an issue. Then, I'm sure that's when people are backtracking, trying to get things in compliance. It's really not the way to do it.

So, what I'd like to do is hopefully we can simplify a little bit of this, what is required, what are some of the basic fundamentals. Maybe first, if you can tell us a little bit more about your legal background and experience involved in this important subject. Maybe you can add your own comments to what I've already shared, about how you see this and the importance in being successful and running your business.

Sherwood: Yes, Scott. I've been doing this for over 30 years. I've held the hands of companies as they've been organized, as they've raised their initial capital, as they've gone public, as they've franchised their operations, and as they've sold or purchased other companies and, ultimately, as they've wound down their operations and dissolved. So, I think I've been involved in almost every aspect of a company's life.

And you're right: it's so easy for an entrepreneur who has a vision of what he or she wants to do, and wants to get out there in the public, starting their operations, and generating revenues, and it's easy for that person to forget that the reason why they organized an entity in the first place is to create some protection for their personal assets, for the assets of the entity that they're creating. It's protection from creditors, from regulators, from disappointed investors.

If you don't cover those details, of course - the devil's in the details - if you don't do those corporate formalities, then you're really jeopardizing your whole operation.

Scott: I agree with that. It is really that serious, it is a subject that needs to be covered. Let's start with the basic fundamentals. We'll just jump right into it.

As you can tell, I want to comment on the side here. Sherwood has extensive experience, as he talked about. At the end, we'll give you some contact information. Definitely, a great resource for the experience of starting, forming, raising capital, all those critical issues, especially in today's economy. Raising capital is key.

Let's start with some basic fundamentals. We'll discuss the importance of corporate and LLC formalities. Can you share with our listeners what are corporate and LLC formalities? What does that mean, and why are they important? What are we talking about when we say that?

Sherwood: Well, typically, when you're talking about corporate formalities, you're talking about undergoing the activities, preparing the documentation to make it very clear that you respect the separateness of this entity that you're working with, separate from your personal life.

The initial organization of the company is started with corporation. It's usually Articles of Incorporation or Certificate of Incorporation, whatever the state requires, the minimum of filing with the state. With an LLC, it's Articles of Organization, or some type of minimal form that's filed with the state. And that's just the first step.

The step that you need to take after that is make sure that your company is fully organized. If it's a corporation, you'd want to have bylaws. You'd want to make sure that you've got directors that are properly appointed initially and ultimately elected by the stockholders. You'd want to make sure that the directors have properly appointed officers.

You'd want to make sure that you've got a stock ledger that shows who the owners of the company are. And depending on state law, you may or may not have to actually issue certificates to the owners.

With a limited liability company, you would want to make sure that you've got an operating agreement. And that operating agreement is basically the agreement between the management and the owners of the limited liability company, that shows what the managers have the authority to do, what the members have the right to do. Also, that operating agreement will indicate who the owners of the limited liability company are and what their rights are as owners.

If you have those documents set up, then you at least have the entity organized properly, so that you could claim that you've got an entity that's separate from your personal life, your personal assets.

Scott: That makes sense. I have a couple thoughts, when you share with that. First is I know a lot of people, in the past, or they have friends and family or fellow business owners that are operating as a sole proprietorship. I know some people might be thinking, "Geez, I know I formed a

corporation. It sounds like a lot of work.” Well, honestly it’s a little bit of work that needs to be done, needs to be done consistently. But my thought is when you’re sole proprietorship, obviously, you have unlimited liability. Sole proprietorship is simple.

I like to say, Sherwood, that simple and asset protection is inversely related. In other words, if you want to keep your wealth and accumulate wealth, Donald Trump doesn’t have one LLC that holds all his real estate. He probably has a very complex structure.

And taking the step to form a separate legal entity is kind of a step in saying, for me, from a psychological viewpoint, I’m looking to be successful. I don’t want to just keep it simple. I realize there’s some other responsibilities; but to be clear, sole proprietorship doesn’t have these requirements, correct?

Sherwood: That’s correct, and I agree with you. Not organizing an entity to keep your business operations is a very shortsighted, almost certain to be regretted decision to make. Keeping it simple initially will really complicate your life later on.

Scott: That’s a good point. The other thought is we get calls from people all the time that the Secretary of States, over the last 5 or 6 years, with technology, have gotten a lot better, in my opinion, they actually figured out they’re actually running a business. So, they’ve made it more user-friendly to go right to a Secretary of State, file the one page of articles.

But, it’s shocking to me as to how many people file the articles and they don’t even have a record book. They have nothing.

Part of the reason, I think that is because what they’re really doing is they’re going to get a check and they talk to the banker. Now, the banker usually depends. It’s interesting with corporations, because usually the

banks don't want to see bylaws but they want to see the operating agreement of an LLC.

So, they form a corporation, go to the bank, "What do I need?" "You need articles, tax ID number, and your personal information. Then you can deposit your check you got to the name of that new company you're going to file." And that's like all they're interested in.

That is kind of a disaster, isn't it, when there's people operating out there with not even any kind of record books or anything. Just filed the one-page state Articles of Incorporation/Organization.

Sherwood: Well, again, the reason why you go through the corporate formalities and keep your minute book and keep your stock ledger and keep your bylaws, is really to demonstrate to the world that you recognize that, "This entity, I respect this entity as a separate entity." And the fewer those things that you do, the less respect that you show to the world that you really have.

If you don't have respect for the separateness of that entity, then regulators and creditors won't have respect either.

So, the more you do in terms of corporate formalities, the higher respect you and the courts and the creditors have for the separate nature of that entity.

Scott: That makes sense. Again, keeping with some of the fundamentals, there are terms we hear all the time. Maybe you can explain the relationship between that comes first. You have shareholders in a corporation, board of directors, you have officers, the LLC. The equivalent might be members, managers, members. Can you explain, maybe from a corporation first, kind of the chain of events, what comes first, second, third? How does that work?

Sherwood: Sure. For a corporation, when you organize a corporation, you file something with the state. Usually, that state will require that establish an initial director. The directors are the managers of the corporation.

The directors initially basically are appointed by the organizer of the entity when they file the document with the Secretary of State.

It's the job of the director to then have a sort of an organizing meeting or an organizing decision to basically say, "Okay, as the organizing director, I am going to reappoint myself as a director. I'm going to add any additional directors that I need to. I'm going to appoint officers." Officers are appointed by the directors.

And then, you're organized. Then, you're started. You've got your bylaws, you've got your board of directors, you've got your officers appointed.

From then on, it's the obligation of the directors to establish the policy for the corporation. And then it's the obligation of the officers, who have been appointed by the directors, to implement that policy.

And after that, it's the obligation of the shareholders to decide who the directors will be from year to year or period of period, or however the term of directors tenure is established in the bylaws of the articles of the company.

You've got your directors that established the policy for the corporation. You've got your officers who have been appointed by the directors to implement that policy, and then you've got the shareholders or the stockholders who own the corporation. They're the ones who decide who the directors will be.

Scott: Very good. Now, what's coming to mind, I know some people are thinking, "I'm a one-person corporation or a one-person, single member, LLC. It might sound kind of crazy. You mean I have to have a meeting with myself? I appoint myself?" Why is that still important? People, I know psychologically, sometimes are thinking, "It's just me." Well, reality is it's not just you. It's a separate legal entity. Can you comment on that, the one person entity that would hold all these hats?

Sherwood: And one person is fine, and it's done often. But still, it's a matter of respecting the separateness of the entity and recognizing that you need to follow the laws of the state. And typically, the laws of the state will require that a corporation have so many directors – oftentimes, it's at least one director – and then, have so many officers.

Then, of course, for the corporation to even exist, there has to be an owner. So, **even though the same person is a director, officer, and stockholder, those have to be clearly designated. It has to be clear that you recognize that, under state law, you satisfy those state laws requirements to have that corporation.**

Scott: Very good. Let me ask you this question, when it comes to running the LLC or corporation. So, you get through the initial formalities. You have the initial minutes, the meetings, the director accepts their position. And correct me on the language. What's the sequence if the director accepts? Do you then appoint the officers? Is that correct?

Sherwood: **Yes, the board of directors appoints an officer in the corporation. In an LLC, it's a little different because, of course, the manager, if there is going to be a manager, is designated in the initial filing with the state. Then after that, the managers are determined in accordance with the terms of an operating agreement.** Usually, the managers are selected by the members; can be removed by the members, the members or the owners.

Whereas in a corporation, you have a separate board of directors and officers. It's the board that establishes the policy. It's the officers that implement that policy.

In an LLC, all of the management is just in the manager. The manager will sometimes establish policies. Sometimes the policy is established in the Operating Agreement. But it's the manager that runs the show and the members are just the owners. Again, that can be the same. But the manager has a different role from the owner/member.

Scott: That makes sense. We'll talk about a corporation first, an LLC. When you have directors, a lot of people, I think, they make an assumption that when they look in a Secretary of State records, they see somebody is the director, the officers, they naturally assume that's the owner. Does that have to be the case or not? Does the director of the company have to be a shareholder?

Sherwood: Not at all. A director does not have to be a shareholder. An officer does not have to be a shareholder. The directors are merely individuals who are appointed by the stockholders to provide management to the company.

Scott: Very good. In an LLC, I want to point this out because there are a couple basic choices when you form an LLC, which is to be managed by managers or managed by members. Can you comment on the difference?

Sherwood: Well, it is an option when you're organizing an LLC. **If you want the persons who are running the LLC to be separate from the members, with separate authority, separate rights, separate compensation, you'll oftentimes have a separate manager. And that manager doesn't necessarily have to be an owner of the company. It doesn't have to be a member.**

But if, for whatever reason, when you're organizing the LLC, you really want the owners of the entity to also be the managers, you can still separate some of the members, so not all of the members are managers. If your members manage it, it just simply requires that if you're part of the management you also have to have an ownership interest in the company.

Scott: That makes sense. I have a certain approach here. You may see it similarly or slightly different. I know especially people raising money, I do have a preference to be managed by managers. And you operate the LLC managed by managers because you might have 2 members, and what if you bring in a third member later, but you don't want him to have management say from day-to-day operations, but they're maybe going to invest money or capital. Do you see that generally as a pattern in a similar way?

Sherwood: I do. My personal preference is to have a manager-managed LLC, rather than a member-managed. I think the roles of a manager are separate from the members. People come in as members in an LLC for different reasons. I just think, ultimately, it's easier and cleaner to organize an LLC when you've got it manager-managed.

Scott: Very good. Before we go into the next one, we're going to talk about what are some things you have to do throughout the year? What are some of the examples of things you should probably be documenting in your LLC or corporation?

You brought up something very interesting earlier, that some people may have heard or not quite heard a lot, is creditors. Or if they do have investors and let's for the moment assume they did everything properly, what are some of the things you've seen over the years, where people haven't done formalities, where they've had investors or things? Does it put the investor, if the investment doesn't go well, in a better position to go after the individual personally? Is that what happens?

Sherwood: Yes. The reason why you organize entities, oftentimes, is to provide protection so that if you're involved in a company, if you've got an investment in a company and you're operating the company, that the creditors of the company can't come after your personal assets if they, for whatever reason, can't collect from the company, and vice versa. Your personal creditors can't come after your company operations, except in limited situations.

If you don't recognize the separateness, and like I say over and over again to my clients, if you don't respect the separateness of that entity, then your creditor's not going to respect that, and courts ultimately or not going to respect that.

So, you keep separate bank accounts, you keep separate books and records. Anything that you can do to make it clear to the world that your company is separate from yourself is going to be to your benefit; creditor-wise, tax-wise, in every respect will be to your benefit.

Scott: That makes sense. So, when the LLC or corporation is up and running, how do you document formal corporate decisions? Can you give an example of something? I've heard things called real meetings with minutes, or paper meetings with minutes, and action by written consent. I don't know if you want to give an example of the sequence of events that should happen.

Sherwood: Scott, what you want to have is some kind of record that reflects that, from time to time, you have reviewed the bylaws of the company to make sure that you're operating the company properly, that the operations of the company are consistent with what your bylaws say the operations of the company will be.

At least annually, if you're a corporation, you would want to make sure that your directors are elected or appointed by the stockholders. You do that via what's often called resolutions.

Resolutions are just sort of a form of a document; a document in which the stockholders elect the directors. And you follow the process in your bylaws for electing the directors. Oftentimes, it just means that you have a consent by its stockholders holding the majority of the outstanding stock, who agree that these people will be the directors for the next year.

In an LLC, there's not quite the same procedure. Oftentimes, a manager will stay in as a manager until the manager is removed. But still, you want even the manager of an LLC to look at the operating agreement from time to time and document the fact that the manager is following the requirements of the operating agreement.

Oftentimes, an operating agreement will require that an annual budget be presented to its members. So, you'd want to document that that budget had been presented and that the members had approved that.

Just some kind of paper to show that you are following the requirements that the corporation or the limited liability company have outlined for the operation of that entity.

Scott: Very good. Is there a term limit for directors? Like you say, we have annual meetings. If somebody is probably thinking, "If I'm the director or we have the same director, is it going to be the same for the year 2 and year 3?" Should they still go through the annual process to appoint and accept that person for the 2nd and 3rd year, even if there is no changes?

Sherwood: Well, I think yes. Like I said, I think, again, it is very important to show that you don't just organize the entity, adopt the bylaws, and then just forget about it; that you document the fact that you have gone through the bylaws periodically. You think it's important enough that you make sure that your operations are consistent with your bylaws. Your bylaws may

say that the directors have to be elected on an annual basis. You don't necessarily have to have a formal meeting, but like I said, you can elect by written consent of stockholders holding the majority of the outstanding stock.

Under Nevada law, and every state law is a little different, Nevada law does not require that you elect your directors annually. But it does say if you don't have a stockholders meeting within 18 months to elect directors, then that stockholder can get a court order to force you to have a stockholders meeting.

It's just good practice to have a regular election of the directors, if you've got a corporation.

Scott: Very good. Let's talk about a couple of examples. Somebody's going throughout the year. They're doing some activities in the corporation. Or there's some day-to-day activities: "I'm going to go to the office supply store and buy paper and paperclips or something," and then they're going to go lease an office or open a bank account or buy \$20,000 worth of computer equipment. When should you have a formal corporate meeting? What are some examples that, throughout the year, you might have some of those? What would be the steps to do that?

Sherwood: Well, I think **when you have to make a decision that's not in the ordinary course of the business, something that's significant, something that has a material impact on the corporation, that's when you'd want to document the fact that, at that point, you're looking at the bylaws to make sure that you know if there's any particular stockholder requirement to approve that particular activity.** If you've got a limited liability company, that there's certain activities that require approval from the members. You'd want to make sure that you get that approval.

That usually occurs if you're buying or selling a significant asset or closing or opening a bank account. Certainly, **if you're changing a director or manager of an LLC. Any significant business event not in the ordinary course of business.**

Scott: Very good. So in my examples, or do you have a couple that come to mind, Sherwood, that would be not in the ordinary course of business, that probably should be documented throughout the year?

Sherwood: Well, I think your example was a good one. If you're going out and buying paper for the copier, that's certainly ordinary course operation. That doesn't need any kind of written documentation for that.

But if you are opening a bank account, oftentimes the banks will not let you open an account unless you can demonstrate that you've got a board resolution authorizing that bank account to be open.

Depending on the size of your corporation or limited liability company, **if you're buying a significant asset like a piece of property, if you're entering into a lease, sometimes a space lease, depending on your operation, may be significant enough that you'd want to have documentation that it had been approved by the directors.**

Scott: Then certainly, your area of expertise, which is securities law and what goes along with raising money and capital, obviously that's all well documented?

Sherwood: Yeah, **there are things that, by statute, has to have approval. For instance, if you're a corporation and you're issuing new stock, the statute says that that new issuance of stock has to be approved by the directors. If you're trying to remove a director, at least the Nevada corporate law says directors can only be removed by**

stockholders. And they have to be removed by stockholders holding at least 2/3 of the outstanding stock.

So, you do need to have some kind of written documentation that you've gotten the proper approval to take that particular step.

Scott: Very good. We'll talk more about that in a minute. You brought up a couple of very good points.

What decisions are made in general by shareholders, versus directors?

Sherwood: The shareholders usually decide who the directors will be. Like I said, it's the directors who establish the corporation policy, but it's the shareholders that elect the directors, that decide who is going to establish that policy. The shareholders are the owners. They're the ones who ultimately control the entity.

Beyond that, most state laws don't specifically require shareholders to approve anything, other than the sale or merger of the business. Beyond that, usually it's left up to the directors to operate the company.

In a limited liability company, the authority of the management is usually established in the Operating Agreement. For the most part, the members or the owners of the limited liability company only select or only have a say in who the manager will be, or whether or not the entity will be dissolved.

One more thing: if there is a change in a document that's filed with the state for a corporation – in Nevada it's the Articles of Incorporation – if there's a change in that document, **any change in an Articles of Incorporation has to be approved by the stockholders. Same thing with the Articles of Organization for a limited liability company. Those have to be approved by the owners of the company.**

Scott: Great example. Let's say somebody has a Nevada corporation and wants to amend the name. So, they're doing an amendment to the articles to change the name of the company. What would be the proper steps for the shareholders? Do they have a meeting? How does that work?

Sherwood: It would be just like any other activity that needs to have the approval. **First of all, the board of directors has to approve that change, and then the board of directors submits it to the stockholders to approve the change.** It can be at a meeting, or it can be by written consent. If it's a board of directors, all of the directors have to approve the activity, if there's no actual board meeting. If it's stockholders, you just have to have stockholders holding a majority of the outstanding stock approve that change, in order to have it accepted and in order to qualify to submit it to the state.

Scott: Very good. We hear the term too, corporate resolutions, versus have a meeting. When can corporate resolutions be used?

Sherwood: Well, **corporate resolutions is just sort of formal name for obtaining consent.** Oftentimes, the documentation that shows that an activity has been approved is in the form of resolutions. "Resolved that the board of directors thinks that the name of the corporation should be changed to something-something," or "Resolved that the stockholders approve the name change of the corporation." That's just sort of the formal name for the approval process, either by stockholders or by a board of directors.

Scott: Can that approval process be done independently or should there have been a meeting by either the shareholders or directors beforehand, and then the resolution is kind of the after-fact summary of what happened?

Sherwood: **The resolution is usually what's presented to get the approval. So, if it's a resolution to purchase an asset, the resolution can be presented at a board of directors meeting.** Well, if it's a purchase of

the asset, usually it's just the board that approves it. So, it's a resolution that's presented to the board. If a majority of the board at a meeting accepts that resolution, then the documentation shows that that particular resolution was accepted by the board by whatever majority, however it's accepted.

If there's not a meeting, that same resolution can be consented to in writing. It's just a document that states the resolution and is signed by those people. If it's directors, signed by those directors who approve it. If it's a resolution submitted to the stockholders, that resolution is just signed by those stockholders who approve it. If it's stockholders, of course, you need to show how much stock each consenting stockholder holds.

Scott: Very good. I'm sure there are some people thinking, listening to this, "I've been in business for 3 or 4 years, had my corporation, LLC for 3 or 4 years. Oops, I've skipped a few of these things." And they're probably thinking in their mind there's a couple major things they did. We'll talk in a minute about changing officers and directors and managers. How do you go back and update records, things that happened in the past? How do you go back and document that to get "your books up-to-date," if they're not so?

Sherwood: Sure. **It's always best to keep your records up-to-date continually. But if you don't do that, if you've made some mistakes or you just got caught up in some other things and you want to go back and make sure that you've properly elected directors, make sure that you've properly approved company activities, then the technical term for that approval once it's already happened, is ratification.**

The board will ratify an activity that really required board approval. Maybe they didn't necessarily get the approval, or maybe they didn't document approval that they had obtained. That board would then ratify the activity that has already occurred.

Same thing with stockholders. Something has already happened and it wasn't properly documented or maybe wasn't even properly obtained, then the stockholders would ratify that activity.

Oftentimes, when a board has to ratify activity, regardless of what that activity is, you still want to get the stockholders to ratify the board's actions.

Scott: Very good. When you do that, is this a resolution minutes meeting? And second part is do you comment in there when this activity occurred, 3 years ago? Then I assume obviously it's dated as of today's date or whenever you sign it, to notify that, "We signed this today, ratifying this is what we did 3 years ago." Is that how that works?

Sherwood: Yeah, my personal opinion is you want to be as clear as possible. Everybody knows that everybody makes mistakes, including corporations and limited liability companies. So, it's no surprise that you sometimes have to ratify actions that weren't properly documented previously.

Be honest. Put in as much detail as you can. Make it as clear as you can, what's happening, what's being ratified, when it happened, what the date is today, when you're ratifying that activity.

And yes, **every action to approve, whether you're talking about approving activities to be done or ratifying activities that have already been done, you typically do it by resolutions. Resolutions either presented at a meeting or resolutions that are in a written consent and signed by those parties who are approving that resolution.**

Scott: That makes sense. Now, what's the language as far as it's a resolution? Is it a resolution to ratify? What does it say in the title?

Sherwood: Well, the title would not necessarily show a ratification. The title would usually be “Minutes of a Board of Directors Meeting.” You wouldn’t know, from the title, what the body would entail. But the resolution itself would just say something to the effect that, “Resolved that the board of directors ratifies the issuance of 5,000 shares to such-and-such a person for such-and-such an amount, determines that the consideration for that stock is fair and just and equitable,” or whatever it is.

The title of the document would simply be “Minutes of the Board of Directors Meeting,” or “Written Consent of the Board of Directors of Such-and-Such Corporation.”

Scott: Okay, very good. Let’s talk about a common subject that happens. Some people start companies, they have a partner. They might be a board of directors. They might be an officer of the company. Some people bring someone in, somebody other than say the spouse or something. They bring somebody in as the secretary of the president of the company, say it was as an LLC’s manager.

Now, it comes time to remove the person. We get calls annually, when people want to update their annual list with the Secretary of State. Obviously, that’s one part of it. We’ll assume everyone is on friendly terms, where the person wants to resign their position. They’ll sign to resign and you’re going to appoint somebody new. Then we’ll talk about what if you have a disgruntled partner. That’s a whole different subject.

But what are some of the steps to go? If somebody wanted to replace a director or a president of the company, what are some of the proper formalities that need to be done to make that official, besides just obviously updating the list?

Sherwood: **My advice to my clients is never bring someone on your board or into your management unless you already know ahead of time how**

you can get rid of them. You've always got to expect that, at one point down the road, there's going to be trouble. So, you need to know ahead of time that you've got the proper authority to remove a director or remove a manager before that director or manager are ever put in place.

If it's a corporation, typically a director will leave by resignation. Just a document that says, "I hereby resign as a director of such-and-such corporation," signed by that director.

Once that resignation has taken place, then you need to go to the bylaws and determine, now that you've got a vacancy, how is that vacancy filled? In most corporations, a vacancy is filled if you want to fill it. Oftentimes, if your bylaws say, "Our board will consist of a minimum of 3 directors," and you had 4, if there's one resignation you still have 3, you may not want to fill that position.

But if, for whatever reason, you want to fill a position that's been vacated, then the bylaws oftentimes will say that the remaining board of directors has the right to appoint a new director to that position.

If that's not the case then, at the very minimum, the stockholders have a right to elect or appoint, by majority rule usually, a new director.

Scott: Very good. You mentioned a very important point about before you bring somebody on, you basically kind of know the exit strategy. What does that mean? Does that mean do they sign documents upfront? How does that work?

Sherwood: **The appointment, election, or removal of directors in a corporation and managers in a limited liability company, for a corporation that process is usually outlined in the bylaws. If not, state law usually covers it.**

For a limited liability company, it's the operating agreement. That's critical. You want to make sure that the operating agreement is drafted in such a way that you know what authority it takes or what procedure it takes to remove a manager if, for whatever reason, a manager is not working out.

So you go to your organization documents and to your state statute to determine what authority, what it takes, what the process is for changing the management.

Scott: That makes sense. What happens if you have a director/officer that – I hear this quite often – they've had issues. The person used the company credit card and they're on a spending spree. "They won't return my phone calls. I want to get rid of them." And they want to update the list of officers. They want to remove him from the company, but they can't even get ahold of the person.

I know this gets into more of a legal issue. But generally, do you have a couple points of what that may entail, if they contacted somebody like yourself? What would be some of the steps that might have to happen so the person can move forward with the company?

Sometimes, both partners have the same story, so that's a different subject. What are some of the steps that might have to happen in a situation like that, that's a little bit more extreme, where you don't have somebody that is willing and able to resign and move on in a friendly manner?

Sherwood: In a situation like that, you go to your organization documents. **Again, the bylaws; the Articles of Incorporation – if you have to – state statute, to determine what it takes to get that person off the board.**

In the state of Nevada, state law is that a director can only be removed if stockholders holding at least 2/3 of the outstanding stock consent to the removal of that director.

Now, you can increase that in your bylaws. You can say that it has to take stockholders holding 90%. But you can't go below 2/3. So, by state law in Nevada, if you've got stockholders holding 2/3 of the outstanding stock, they can remove the director.

Scott: So, if you're 50/50, is that a problem then?

Sherwood: If you're 50/50, that's a problem. **If you're 50/50, then if that director doesn't resign, then another option is, following the process for electing directors, you have a meeting of shareholders, and in that meeting of shareholders the new board is elected.**

If you've got a 50/50 ownership, you've got a problem. But if you've got a majority of the outstanding stock at a meeting of stockholders electing a new board of directors, you simply elect a new board of directors that doesn't include the problem director.

If that doesn't work, then ultimately you're going to have to go into court and get some kind of court assistance in resolving whatever problem exists.

Scott: Like you mentioned, 50/50 with an outside partner can be a challenge. As long as we're on that subject for a minute, if you do have an outside partner, you'll hear agreements like a buy-sell agreement, shareholder agreement. There are different purposes for those. Does that help solve this issue, per se, or is that still just a separate subject?

Sherwood: Well that does, but it requires one partner being willing to buy out the other, which sometimes is difficult, and sometimes is just totally impossible.

Oftentimes, within the bylaws or the operating agreement, you will have deadlock procedures. If there's a deadlock on the board or a deadlock among the managers, you will have a procedure for breaking the deadlock, whether it's giving super majority vote to one or the other, tossing a coin, bringing in a third party.

If you've got a 50/50 ownership, that's something you've got to recognize is probably going to occur in the future. So, **it's critical that you set out ahead of time how that deadlock is going to be resolved.**

Scott: Very good. Then the other thought that comes up is people that have issues, typically what happens is, "Well, let's just make all this go away." And their thought process to make this all go away is, "Let's dissolve the corporation or dissolve the LLC."

Can you comment 2 things: what it takes to make that happen? Then number 2, there are some ramifications in the statutes about ongoing liability for a period of time. If you can comment about that second. I think some people think it's a magic wand to make problems go away, and it just doesn't quite work that way.

Sherwood: No, it's not. Dissolution again, that's something that requires approval of the members. It's obviously a significant step that the corporation or the limited liability company will take. Any significant step can't be done without stockholder and member approval.

The fact that you're in a deadlock may stop you from taking that option and may force you to go into court and ultimately have a court determine that, "This is just not going to work. This entity needs to be dissolved."

And, as you suggested, **when you dissolve an entity, it's not as if you can just say, "This entity is dead. And since it's dead, creditors or litigants are just out of luck."**

No. In fact, the management of the limited liability company, the board of directors, they basically are still responsible for making sure that the debts and obligations or any claims against the entity are satisfied for at least 2 years, possibly longer, if there's a court that orders a longer period.

There's still a substantial amount of time in which any problems that exist in that company are going to have to be resolved by the company's management.

Scott: A couple of quick thoughts come with that. Then, I have a couple other questions. Why don't we do this first, because I know people are already thinking, "I need to contact you," and they need to talk to you about their situation. What are the fees and costs to get things up to speed, properly go back and execute on a few things that maybe weren't done properly, especially if they had people come and go.

What's the best way to get a hold of you and your firm, Sherwood?

Sherwood: Well, I'm in Las Vegas. My office number is (702) 870-6060. Durham, Jones & Pinegar. You can check us out on the website. Contact us through the internet as well.

Scott: Very good. So again, it's Sherwood Cook. The phone number to contact him at his firm is (702) 870-6060, based here in Las Vegas.

Some people who are listening to this call are going to be in different parts of the country, incorporated in different states. In your licensing activities, what areas can you handle in a Nevada-specific area? I know securities is different. Can you comment about what would be or maybe a situation that you wouldn't be able to handle, they should go to a local attorney just because it's state specific?

Sherwood: Yeah, it's a situation that you have to look at on a case-by-case basis. Sometimes, I'm very comfortable resolving a problem that didn't

necessarily generate from a Nevada organized entity. But it just depends on the situation.

Scott: Sure. So best approach is give Sherwood a call and he'll review that with you. Then, you can kind of go through fees and things of that nature. Now, if somebody needs to update formalities, maybe they had a couple annual meetings and things?

Sherwood: **Those are pretty easy, and those can be taken care of by a legal assistant.** So, those are not going to be quite so difficult as if you're trying to resolve a problem with who owns what and who has the authority to do what. That's a little more difficult.

Scott: Yeah, that makes sense. So going back to dissolving the entity, what's Nevada's percentage as to who has to agree in I should say shareholders before a dissolve?

Sherwood: For a corporation, it has to be a majority.

Scott: So a majority would have to agree. Again, that's where you get into the issue of if you have a 50/50 owner and they're not willing participants dissolve.

It also sounds like you could also perhaps shoot yourself in the foot that for some people that still have debts and issues. Is sometimes it a better approach to stay in business and not dissolve and figure out a way to settle those things before you dissolve it?

Sherwood: Absolutely. **Just like any other decision, you want to know ahead of time what the possible problems will be. In a dissolution, any outstanding claims, any outstanding creditors, are a real problem.** They have to be taken care of. And if they're not taken care of properly, then that leaves the management and possibly the owners open to a personal liability. That's exactly what you don't want to have.

So, before you dissolve the entity, one of the things you want to make sure of is how are the creditors going to be taken care of.

Scott: Very good. Let's finish with a couple thoughts about when you do have partners, about a buy/sell agreement, a shareholder agreement. When should you have those in place? And what's some of the negative consequences that could occur if you don't take the time?

I know from our experience talking to people, we bring it up to them, "Yeah, yeah, I'll get to it." They're off and running, a year goes by, they never did it, of course. And then now they have issues, and it just seems like clockwork, they're like suing each other.

And whether somebody wants to leave or not leave and how much capital they put in and was it a loan or not. I mean there's so many things that are just it's like everybody develops amnesia. So, that's why we need to put this stuff in writing. What are your thoughts on that?

Sherwood: Something like a buy/sell agreement, that's where one party buys out another, that occurs when there's a deadlock, discord, or even death. That's something that's really critical when you've got a 50/50 ownership. It's just one of those situations that it is always easier to take care of now, rather than later.

When you're first organizing an entity, when you first got cooperation and excitement among the partners, that's when it's most likely that you can resolve this issue of what, "Happens down the road, if there's something that requires us to go our separate ways?" If you wait, the longer you wait, the more difficult it's going to be to get cooperation, to get a meeting of the minds, to ultimately resolve all of the issues that need to be resolved in a buy/sell agreement.

It's one of those things that it's a detail that you don't want to take care of in initial stages, but it's a detail that if it's not taken care of initially, it's only going to be more difficult to take care of later on.

Scott: I agree with that 100%. My thought is, too, **if you're at the euphoria of the excitement of your great vision, and you're with a partner, and you bring up a buy/sell agreement and talk about what happens if somebody wants to leave, if the other partner is not willing to invest part of the start up capital to get these things in place properly, and they don't want to do it for whatever reason, usually that's always a flag.**

Sherwood: It's a big flag. And it's just like a prenuptial agreement in a marriage. It's horrible to think of the possibility of this wonderful relationship that's taking on this great new adventure together, it's horrible to think of the possibility that there would ultimately be a divorce. But statistics and common sense will tell you that there is a very likelihood that ultimately the breakup is going to occur.

So, best time to prepare for that horrible event is now, as soon as possible.

Scott: That makes a lot of sense. We'll comment on one – as we finish up here – you mentioned, which obviously does happen, is what happens if your partner dies, and then their estate gets involved. And they're expecting, "What's our value worth, and when do we get a payout, and we don't want to be a partner, but we'll take our money please." That's an issue, too, right?

Sherwood: That's a big issue, death or disability. That's a big issue, and you'd want to take care of that as soon as you can.

Scott: Wonderful. So, take the next step. **You've probably heard several things throughout this call that you probably haven't been in compliance, probably need to ratify a few things. You maybe had a partner before, maybe you're in a company that's been successful, the partner, and knock on wood, everything's still good. You see you probably need to take the next step to formalize some things before things go any further.**

Also, you might be in a situation where you're looking to raise capital, and that's a very serious subject that needs to be done properly. Sherwood is definitely the expert on that, agreements and things to go in place before you even think about going out and looking for investors or some things.

Any of those situations, I recommend you call Sherwood Cook at his offices. He is with the law firm Durham, Jones & Pinegar. His phone number is (702) 870-6060.

Sherwood, any final thoughts today?

Sherwood: No, Scott. I appreciate being here.

Scott: Yeah, I appreciate you taking the time to be with us and help out our members to be in compliance. Thank you very much for all your energy and input, as always.

So, thank you everybody, and this will end the call for this evening.

And if you do have questions, of course, you can contact our company, Nevada Corporate Planners, at (888) 627-7007.

Again, everybody have an outstanding evening. And this will end the call for tonight.