

# OPERATING AGREEMENT



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LEGAL

# Operating Agreement Overview

**WHAT IT IS:** This is an agreement laying out the rules of ownership among the members of an LLC. If it is a single member LLC, then it's largely a formality to show 100% ownership and to maintain necessary corporate formalities. If the LLC has multiple owners, then it requires more attention as it is an agreement between the owners.

**WHAT IT DOES:** This agreement sets expectations and outlines terms for the owners. Most notably,

- Name of Members and their ownership of the company
- Decision Making Rules
- Money protocols such as profit/loss allocations, distributions, and capital contributions
- Dispute protocols

**WHY YOU NEED IT:** To show either your sole ownership in a single member LLC (this also helps if you get sued to maintain your corporate veil) or the allocation of membership if you are a multi-member llc. It also helps prevent misunderstandings and disagreements among the owners.

**WHEN TO USE IT:** When you register an LLC whether multi member or single member.

# Clause-By-Clause Explanations and Instructions

The following explanations detail exactly why each clause is in this the agreement and what you need to do to edit it to your needs. As mentioned in the video, I highly suggest that multi-owner LLCs work with an experienced business attorney as soon as it makes sense for the business and the budget. There are a lot of customizations that a lawyer can provide that simply cannot be addressed in this document; however, it does a great job of detailing the meat of what's needed. So spend a few extra minutes to get to know your agreement and customize it accordingly. Of course, reach out to us with any questions and we'll be happy to provide help.

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**Editing Instructions:** Sections that should be filled in, altered to suit your needs, or deleted if they're not applicable to you are in **red**.

## The Title

On the top of the page, insert your business name in **[Company, LLC]**. Insert the **Date Agreed Upon** at the top of the agreement.

## 1. Formation

**Purpose:** The clause starts everyone off on the same page. The purpose of a formation clause is to establish the purpose of the agreement. Here, the clause states that this agreement will serve as the operating agreement for your Company, and it states that all signing members will be required to abide by the following terms.

**Instructions:** Insert your Company name in Name of Company.

## 2. Members

**Purpose:** This clause is the space where you list all the signing members of the operating agreement. Additionally, this clause specifies what ownership percentage each member has along with their individual contributions.

**Instructions:** Add all member names in the space provided. Add each member's ownership percentage and contribution as well.

## 3. Purpose

**Purpose:** What is the purpose of this business? This clause clarifies your Company's business purpose, and it gives the Company the right to carry out its responsibilities and activities.

**Instructions:** Insert your business purpose in the [insert business purpose.]

## 4. No State Law Partnership

**Purpose:** No state law partnership clauses verify that the business being formed is a limited liability company (LLC)--not a partnership. State laws and taxes treat these businesses separately, so this clause is used to clarify that your Company is a LLC. This also prevents you from being liable for acts of your partners (ie maintains the liability protection you are looking for with an LLC).

**Instructions:** None.

## 5. Decision-Making

**Purpose:** Your Company will inevitably be faced with hard decisions to make. Per this clause, all members should intend to try to reach consent on all decisions. However, in the event that there is not unanimous consent, a majority (51%+) vote from the members will decide the course of action.

**Instructions:** Be intentional about your decision-making structure. Review whether majority vote is consistent with your LLC. If not, be clear with your agreement among members and include in this section.

## 6. Unanimous Consent

**Purpose:** Certain decisions that your Company must make should be determined by unanimous consent of your members even if the day to day operations are majority vote. Unanimous consent means 100% of the members agree in a vote. The actions listed out in this clause specify what votes require unanimous consent to be passed.

**Instructions:** Are there any others that you would want unanimous. If so, consider adding to this section.

## 7. Capital Contribution

**Purpose:** Capital contributions are cash or assets given to an entity in exchange for an equity interest. Here, members are not required to make additional capital contributions.

**Instructions:** None.

## 8. Profit and Loss Allocations

**Purpose:** Profit and loss allocation clauses explain how members get paid with profit or assigned with loss. Here, the clause is designed for members to be proportionally allocated profit and loss based on their membership interest described in Section 2.

**Instructions:** None.

## 9. Distributions

**Purpose:** The distributions clause deals with the timing of when members get paid. Here, it is up to the majority of members to decide the time frame. How money will be handled is integral to the business and, importantly, the relationship among the owners. This is part of your regular communication so be sure to discuss this from the outset and on an ongoing basis. You need to consider things like whether money will be reinvested into the business, when will salaries being to be paid, when will distributions be made. Your needs will be evolving so you will need to start on the same page and remain on the same page. Communicate frequently about this.

**Instructions:** None.

## 10. Intellectual Property

**Purpose:** Intellectual property is defined as intangible creations such as trade secrets, industrial design, and rights associated with a patent or trademark. Here, this clause gives the ownership of intellectual property to the Company for business purposes.

**Instructions:** Include any IP of a member that is specifically excluded so that it is clear.

## 11. Limitation of Liability

**Purpose:** This clause explains that members are not personally liable for business decisions so long as the business decisions are made with the best interest of the business in mind and in “good faith.” This term gets thrown around a lot in the legal world. It boils down to this question, did the member make his/her decision honestly, fairly, and lawfully? If so, the member is not personally liable. Things like stealing money or fraud would not be protected but otherwise there would not be personal liability for decisions pertaining to running the business.

**Instructions:** None.

## 12. Indemnification

**Purpose:** An indemnification clause assures that your Company will defend your members against all claims brought against them related to their role in the Company--so long as the member was acting in good faith. To indemnify means to “defend” or “hold harmless,” so here, the Company agrees to cover a member’s lawsuit related fees if they are sued in connection to the Company.

**Instructions:** None.

## 13. Dispute Resolution

**Purpose:** This clause is a three-step process to how members will handle conflict resolution issues. First, everyone must make a good faith issue to resolve the issue. If that doesn’t work within 30 days, all members in controversy must pursue mediation to solve the issue. If mediation is unsuccessful, arbitration is the last step. Arbitration is an effective legal process that will determine how the members will settle their dispute. Read the clause carefully to determine how to choose mediators and arbitrators.

**Instructions:** None.

## 14. Governing Law

**Purpose:** This clause clarifies what laws will govern this contract. Contract laws vary state-to-state, so the contract must clarify what state laws govern this particular agreement.

**Instructions:** Replace [STATE] with your state where you are filing your articles of organization.

## Signatures

**Purpose:** Finality. Without actually signing it, there will not be clarity on whether final agreement was reached.

**Instructions:** Sign it and save a copy.

# Optional

## Value Proposition / Mission Statement

This is not a legal or even binding, but I think this is a good business practice as well as an guiding principle when difficult decisions need to be made. Try to sit down and create this. If not, then skip it.

## Duties and Responsibilities

I think this helps with clarity among business owners. Just a simple list of who is doing what. This can help prevent some early power struggles and improve efficiencies.



# EIN Instructions

## 1. Decide Whether You Need an EIN

The answer is likely yes. If you have employees, then yes. If there are multiple owners, then yes. If you are a single member LLC, then maybe. We tend to lean towards going ahead and getting the EIN. It will limit you having to share your SS number and further separates your business. Also, some banks require it.

## 2. Only use IRS Website

Link to the IRS Website with information and an online application form: <https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online...>

If this link has changed, you can also google this. Just make sure you are on the IRS “.gov” website. And do not pay or provide your private information unless you are certain it is the IRS website.

The entire process should take about 5 minutes to complete and you will get an EIN instantly. You do need to wait until your LLC has been filed so that you can use that information.

