Setting Up Your First Business Entity

Sarah Sawyer: Welcome to This Week's OK at Work with myself, Sarah Sawyer, and my colleague Russell Berger, both attorneys at Offit Kurman. And today we are talking a little bit about entity structures and formation and what to do when you're starting a business, at the beginning phases.

So there are a lot of different things that can come into focus when you're trying to figure out, "All right, I want to start this business. I want to do this really cool thing. I can't wait. I've got these partners in place. We're going to operate in a couple... You know, my friend's in New York, and I'm in California, and we're going to do this business together, and

It's going to be great, and let's just get going and let's start. And let's Just file an LLC, the paperwork online, and then we'll just go ahead and get started on this business," right? I mean, I'm being a little simplistic and a little silly obviously in setting up this example, but obviously there's a lot of things on that ground level that business owners really need to be... or prospective business owners, if it's their first business, need to be [00:01:00] thinking about when they get started. So what are some things that are top of mind, top of that list, Russell, for someone when you've got a good idea, maybe you're going to include some other people, maybe you're operating in different places.

What should people be thinking about?

Russell Berger: Yeah. Well, an initial question here is probably one for an accountant. What entity should I form? How does it impact taxes? So that's usually a good place to start because, most people are inclined to minimize their tax burdens. And maybe depending on the type of business, if you're really ground floor starting, it might not make any difference, but, it's worth a conversation with an accountant to get that piece of it sorted. From there I think there are preliminary questions that you should discuss with a lawyer about like you said, what state are you in?

How big are you? What type of business are you going to be? What are your plans for expansion and growth of this business? Are you going to grow the ranks of ownership? Are more people going to join? Is that something, a feature you want to build in from the start? So I think all those questions go into the like what are we forming and how should we form it?

And then [00:02:00] once you get a handle on that, you get to the next phase, which is, really like these initial documents, which you should definitely have. If you're going to have a co-owner, don't just go to the state and file and start. That's a recipe for disaster later on.

But when you do form this entity and you create your documents, it's really a roadmap for, how are we going to get together? What is the deal of our partnership? How are you going to live together while we're operating this business? And to the extent we break up at any point sometimes that's for good reasons.

Maybe it's an exit of a sale. But, when we break up this business or when one of us leaves or one of us retires, what does that look like? What's the roadmap for offboarding one or more owners?

Sarah Sawyer: I think also having conversations around the risks that you're taking on as a business, right?

So insurance is a big piece that people get when they first start a business. Depending on what type of business it is, you might need different types of insurance, you might be taking on different types of risk. And depending on the entity [00:03:00] structure and how everything is structured, there might be different levels of risk that people are taking.

And really walking through and understanding, well, what are the, downstream challenges that we're gonna face? How are we gonna address those? How do we wanna protect ourselves? Getting on the same page, 'cause everyone's got different risk tolerances as it relates to how much risk they're willing to take on, how invested they're willing to be in these businesses.

And so understanding kind of what everyone's risk profile is, where there might be disagreements on offloading some of that risk because obviously there's a lot of different risks depending on industry, for instance, right? If you're making widgets versus if you're providing services or just how much of a target might you be depending on, what that is.

So it's not really the sexy, fun part necessarily to talk about at the beginning of a business 'cause no one likes to think about necessarily how it's gonna go wrong or where that risk is or how risky that business is. But that's something I've seen with my clients sometimes also is well, maybe you can't insure certain things that you thought you were going to [00:04:00] be able to.

So I always like to mention that as well as you're putting that structure together because that's something I think people overlook in that beginning phase as well.

Russell Berger: Yeah. Well, and that's a really good point 'cause, again, this is highly specific to whatever you're creating, whatever you're doing with these organizations, but, you might be able to create kind of a multilayer organization.

One entity has all the workers in it, one entity owns the real estate. There are complex corporate structure, and obviously if you're starting out, you don't necessarily think like, "Well, I should have a complex multilayer corporate structure." But sometimes that, it might not be that complex, but having something more than just a single entity might be the right way to lay off some of the risk.

Sarah Sawyer: Yeah. No, great advice. Well, thanks Russell, we'll see you next time.

Russell Berger: Thanks, Sarah.