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## Nevada LLCs:

### Why You Should Review Corporate Structure to Avoid the Alter Ego Doctrine

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***It is important to review your structure from the very start, not once a problem arises.***

If you are a business owner of a Nevada LLC, Nevada provides a lot of benefits. However, it is more important than ever to review your LLC

structure to ensure the LLC does what you think it does.

LLCs generally provide limited liability protection to their owners because typically, owners are not personally responsible for business debts and liabilities of the LLC. As a result, creditors usually cannot pursue owners' personal assets to pay business debts. Business owners also stand to gain many other benefits when they form a Nevada LLC.

Key benefits of an LLC include: Income/loss is passed through to the owners' personal tax returns and any tax due is generally paid at the individual level; no ownership restrictions as LLCs do not face restrictions on the number or type of owners; flexible management; owners have flexibility in structuring company management; fewer formalities because LLCs have less annual paperwork than C Corporations and S Corporations and; credibility because LLCs may be perceived as a more legitimate business than a Sole Proprietorship or General Partnership. But, businesses should keep in mind that LLCs are still subject to ongoing filing requirements of the State, such as filing Annual List and renewing the Nevada State Business License and paying the applicable fees. There are several penalties for missing filing deadlines – and your business could even get revoked by the State.

One of the primary purposes of forming a Nevada LLC is the existence of a liability veil, which means the LLC is treated as a separate entity and members or managers of the LLC are not held personally liable. The Nevada Supreme Court has not yet addressed whether the theory of alter ego applies to LLCs. However, according to The National Law Review, S. District Court Judge Kent J. Dawson recently predicted that the Nevada Supreme Court would treat an LLC as a corporation for the purposes of applying the “alter ego doctrine” and holding managers and members personally liable for debt of the LLC. Moreover, several lower courts and the Federal District Court in Nevada have implied that an alter ego doctrine would apply to LLCs.

Over the past 30 years, the corporate veil in Nevada has only been pierced twice by the Nevada Supreme Court. In both cases, the Nevada Supreme Court pierced the corporate veil to protect a party from harm through fraud because of poor company operations, noncompliance with corporate formalities, or co-mingled assets.

In fact, in the 19th century, courts began to have an exception to this principle for corporations, using the alter ego doctrine.

However, the exception was not originally applied to LLCs because they did not then exist. So, with the creation of LLCs, courts have had to confront the question of whether the alter ego doctrine can apply to LLCs. NRS 86.371, provides: “Unless otherwise provided in the articles of organization or an agreement signed by the member or manager to be charged, no member or manager of any limited-liability company formed under the laws of this State is individually liable for the debts or liabilities of the company.”

Judge Dawson's ruling notes NRS 86.371, but views the alter ego doctrine as an unexpressed exception to the statute. NRS 78.747, governing corporations, similarly immunizes stockholders from corporate liabilities “unless the stockholder...acts as the alter ego of the corporation.” Therefore, LLC members and managers should certainly anticipate that Nevada Courts will apply an alter ego theory to LLCs at some point in the future.

As you consider forming and operating an LLC in the state of Nevada, there are some key facts you should know to limit the likelihood that a third party creditor will “pierce the veil” of an LLC's liability protection. First of all, when using the name of an LLC, the name must always end with “Limited Liability Company,” “Limited Company,” “Limited,” “LC,” “Ltd. Co.,” “Ltd.,” “LLC,” or “L.L.C.” The name must not be the same as the name of any other Nevada Corporation, Limited Partnership, Limited Liability Company or other entity. In addition, it is essential that LLC formalities (although limited) should be followed, including Secretary of State Filings and minutes for annual or special meetings. An Operating Agreement for the LLC should be prepared and signed by its members. LLCs should be properly capitalized and obtain adequate insurance. Perhaps most importantly, LLC assets, expenses, and revenue must be constantly maintained and accounted for separately from the personal asset expenses and revenue of its members.

*About the Author: Lance McKenzie is a partner in the Trusts & Estates and Business Entities & Transactions Groups with McDonald Carano. Mr. McKenzie's practice focuses on sophisticated estate tax planning and estate administration for high net worth individuals and businesses, including strategic planning strategies for asset protection, gift tax planning, probate and trust administration, charitable and private foundations and business transactions. His practice also encompasses transactional work including entity formations, structuring buy-sell agreements, corporate and asset acquisitions and reorganizations.*