

An Overview of Corporation Law

The Maryland State Department of Assessment & Taxation (SDAT) regulates the administrative process of filing and maintaining a corporation, limited liability company (LLC), or other legal entity. This is quite distinct from what the laws of the State of Maryland require to legally form and maintain the existence of such an entity. SDAT does not provide individuals with any legal advice, and therefore their forms satisfy only the most *minimal* legal requirements and do not necessarily afford the full scope and breadth of protection permitted under law.

Entities exist under law really for one purpose: to insulate the individual shareholders, directors, members and/or officers from personal liability so long as the entity is properly maintained and operated.

Corporations

To exist as a **CORPORATION** complying fully with the laws of The State of Maryland, a corporation must have at minimum:

- 1) Articles of Incorporation;
- 2) Bylaws;
- 3) Organizational Minutes; and
- 4) Stock Certificates issued

SDAT as a *regulatory agency* only requires the filing of Articles. The other documents although internal documents of the corporation are required to exist by law. These documents are also often required to transact business and in legal proceedings.

Sometimes accountants will create and file corporations for clients, but most often and best-suited to the task are attorneys. This is

because lawyers are trained to read and interpret the law and understand the *legal* requirements based upon your particular circumstances. Thus it is always advised to *first* seek the advice of a competent lawyer before filing for your entity.

The Number One Rule is that you are NOT the corporation. You may own either a *share* of the corporation or *all of the shares* of the corporation (also known as *stock*); but it is not you, and you are not it. An entity has its own legal existence under state law. It also has its own tax identification number issued by the IRS (employer identification number or “EIN”) just like you have your own social security number. An entity is a separate legal thing with its own life and its own separate bank account.

Stock vs Non Stock Corporations

NON STOCK CORPORATIONS exist for the sole purpose of having a non-profit or charitable organization and further requires that you subsequently qualify as a tax exempt organization with the IRS. A NON STOCK corporation by definition has no shareholders, and the business is overseen by a Board of Directors. Businesses that intend to make money for the benefit of individuals should not file as NON STOCK just because they wish to donate money to charity, or to afford a tax deduction, or to avoid paying taxes. This is complex process and should be properly researched.

Close Corporations

The law requires that a Corporation has:

- 1) Shareholders;
- 2) Officers; and
- 3) a Board of Directors

This sure is an awful lot of oversight for a small business operation! The law therefore permits you to relax some of these and other formalities by electing to be a *close* corporation (*not* “closed”). Think of it also as a *closely-knit* group of people; like “mom and pop” operations.

Practically speaking, the main benefit of a CLOSE CORPORATION is that you get to relax some of the formalities such as abolish the Board of Directors and simply control the business and affairs by your percentage ownership of stock.

Keep in mind that to qualify as a CLOSE CORPORATION and abolish a Board of Directors you must:

- 1) elect to do so in the Articles;
- 2) name *initial* director(s); and
- 3) then abolish the Board of Directors

Limited Liability Companies

LLCs are relatively new entities under Maryland law, coming into existence only in 1992. LLCs are not considered to be statutory entities because the statutes---the laws---do not govern how they operate. Instead what controls the operations is a contract amongst the parties called the OPERATING AGREEMENT. This is a complex document comparable to a partnership agreement that must provide for every “what if” circumstance in the life of the company and it therefore can be costly to draft. Although it is not required to be in writing, it is always advisable to have contracts in writing to confirm the agreement between the parties. Also, instead of shareholders, LLCs have MEMBERS.

Here again, what you file with SDAT does NOT satisfy the legal requirements. The law requires an LLC must have at minimum:

- 1) Articles of Organization (to SDAT);
- 2) an Operating Agreement; and
- 3) Member Certificates

There is still much debate amongst professionals over whether and when to use an LLC vs. a corporation and it is therefore advisable to consult with a lawyer to choose the proper legal entity based upon your intended business use and circumstances.

Forms Provided by SDAT

The forms provided by SDAT for formation of entities lack much of the “magic legal language” which may among other things expand your protection from personal liability. How you fill out the forms has both legal and tax consequences.

Internal Revenue Service and Taxes

The Internal Revenue Service requires that you obtain an Employer Identification Number (EIN) for any entity, whether a corporation, LLC, or otherwise—a tax number for the entity.

There are additional annual filings required with the IRS for either form of entity and certain amounts of income and expenses may also affect your personal taxes. Certain tax designations must be chosen and filed with the IRS within 90 days of formation thus it is best to consult with a tax professional who can advise you as to such elections.

Personal Property Return

SDAT requires an annual PERSONAL PROPERTY RETURN to be filed by every entity,

together with an annual fee. Any taxes due will then be assessed.

Failure to file your Personal Property Return and pay all taxes and fees will result in the forfeiture of your entity and accordingly loss of protection from personal liability.

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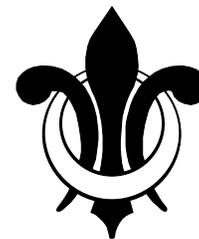
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A Legal Guide to Maryland Corporations & LLCs

*The Law vs. SDAT
Administrative Requirements*



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