

Strictly Business

A Business Law Blog for Entrepreneurs, Emerging Companies, and the Investment Management Industry.



ABOUT THE AUTHOR

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In his corporate practice, Mr. Davie has worked extensively with his clients on all aspects of their businesses, including company formation, business planning, mergers and acquisitions, vendor and customer contracts, corporate governance, debt and equity financings, and securities offerings. In addition, he has represented investment advisors, securities brokers, hedge funds, private equity funds, and real estate partnership syndicators in numerous private offerings of securities and in ongoing compliance. Prior to returning to private practice, Mr. Davie served as the general counsel to a private investment fund manager.

In his real estate practice, he has participated in property acquisitions, mortgage financings, and commercial leasing matters throughout the United States. He has represented developers, governmental entities, life insurance companies, banks, and owners of malls, shopping centers, industrial parks, and office towers. He has worked on a number of transactions involving the syndication of real estate partnerships, advising sponsors on both real estate and securities issues.

Should new business owners incorporate in Nevada?

Previously, [I wrote](#) about the pros and cons of incorporating in Delaware as a small business owner. My conclusion was that, for most small companies, the disadvantages outweigh any advantages. In this piece, I'll cover my thoughts on another state that is frequently pitched as a good place for incorporation: Nevada.

Like Delaware, Nevada has a special court system for litigating business disputes. Nevada promotes its so-called "Business Court" as efficient and fast in its case management. However, Nevada's Business Court doesn't issue written opinions or binding precedent, so it does not provide the predictability that Delaware provides. In addition, as with being incorporated in Delaware, if your business is physically located in a state other than Nevada, the supposed efficiencies are probably outweighed by the hassle of having to litigate cases in a far away state. Therefore, for most business owners, I do not see Nevada's Business Court as being a major benefit.

The second big selling point to incorporating in Nevada is that Nevada supposedly has greater protections for shareholders against a "piercing the corporate veil" action. Piercing the corporate veil involves holding the owners of a corporation or limited liability company liable for the debts of the company. Generally, piercing the corporate veil can only be done in extreme situations such as when the shareholder commits fraud or when the corporation is deemed the "alter ego" of the shareholder. The standard for successfully piercing the corporate veil in Nevada may be stricter than in your home state. However, it is important to note that if a lawsuit takes place in your home state or in some other state besides Nevada, conflicts of laws principles may cause the law of a state other than Nevada to control whether a piercing the corporate veil action would be successful. In other words, judges often have a lot of discretion as to which state's laws apply in multi-state cases and often begin with the assumption that the law of the forum applies unless a party can show that other state's laws have greater contacts or interests in the case. In fact, while Nevada corporations are often promoted as being



particularly useful to business owners in California, California has been one of the most aggressive states in applying its own corporate laws to businesses incorporated elsewhere but doing business in California. Therefore, my recommendation is to use your own state's incorporation statute and take effective precautions against liability, which includes observing all corporate formalities and making sure that you and your company have adequate liability insurance coverage.

Nevada corporations are also promoted for their asset protection abilities. Nevada law provides that the sole remedy available to creditors of owners of Nevada closely held corporations and LLCs is a charging order. A charging order is an order by the court directed to the company ordering the company to send all distributions and dividends that would have gone to the shareholder/owner/debtor to the judgment holder instead. This limitation can make it more difficult for a creditor to collect on their judgment because the creditor will not be able to force the debtor to sell their stock or ownership interest in the company. Usually, after a creditor obtains a judgment against a debtor, the creditor is entitled to sell the debtor's personal property to satisfy that judgment. However, if the creditor's sole remedy is a charging order, then the creditor is entitled to whatever distributions or dividends are produced from the ownership interest (if any at all), but the creditor cannot transfer or sell that ownership interest. Having this protection can give a debtor more leverage in negotiating a settlement. However, the charging order limitation is not unique to Nevada. Most states' LLC statutes provide that the sole

remedy to a creditor of a member is a charging order. It is true that Nevada has extended the charging order limitation to situations that other states have not, namely to closely held corporations and single member LLCs. However, as in the case of piercing the corporate veil, you cannot be sure that your own home state won't go ahead and apply its own law to the situation, notwithstanding whatever Nevada law states. My colleague Jeff Vandrew [wrote recently](#) about this issue and has [some suggestions for alternative asset protection precautions](#) that can be taken using your own home state's LLC statute. These precautions are far more likely to accomplish your asset protection goals than simply incorporating in Nevada and hoping that the judge applies Nevada law.

As with Delaware, I don't think there is much advantage for most businesses to incorporating in Nevada, as opposed to the business owner's home state. You will end up incurring double the fees, because you will have to pay Nevada's fees and then pay your own states fees to obtain authorization for your Nevada entity to do business in your own state. Despite this additional cost and complication, it is uncertain whether you will see any of the benefits, such as greater asset protection and liability protection, that are often promised in connection with incorporation in Nevada. As always, your final choice in entity selection should be based on your own specific situation. Therefore, before making any final decisions on your form of business, you should speak with your attorney.

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