

## What in the World is an LLC? What You Need to Know About Businesses & Law

There are many reasons why people choose to create a corporation, partnership, or other business entity, and one of them is to limit risk of losing personal assets. In North Carolina, as in other states, there are several different kinds of business entities, and knowing what they are is a good place to start.

<i>Corporation</i>	GS Ch. 55	(Inc., Corp., Ltd., Co.)
<i>Professional corporation</i>	GS Ch. 55B	(P.A., P.C.)
<i>Non-profit corporation</i>	GS Ch. 55A	(Inc., Corp., Ltd., Co.)
<i>Limited liability company</i>	GS Ch. 57D	(LLC)
<i>Limited liability limited partnership</i>	GS Ch. 59	(LLLLP, RLLLLP)
<i>Limited partnership</i>	GS Ch. 59	(LP)

---

---

---

All of these entities are “artificial persons” under the law, meaning that they have the ability to contract, sue, and be sued (through their agents, of course). With few exceptions, people who own part or all of one of these business entities are not personally liable for debts or other liability incurred by the business.

All of these forms of business are required to register with the Secretary of State’s Office and to maintain a registered agent for the purpose of receiving service. In its instructions for forming a North Carolina corporation, the Secretary of State’s Office says:

*The registered agent for your corporation can either be an individual or another business corporation, nonprofit corporation or limited liability. If the registered agent for your corporation is an individual, that person must reside in North Carolina. If the registered agent for your corporation is or another business corporation, nonprofit corporation or limited liability company, it must be active on the records of the Department.*

*The Registered Agent must have a Registered Office. The Registered Office is the business address for the Registered Agent. The Registered Office must be located in North Carolina and have a physical address. You have to list both a mailing address and physical (geographic) address for your Registered Office if they are different. You must give a correct street address for your initial Registered Office.*

*The only duty of the registered agent is to forward any notice, process or demand that is served on the registered agent, often by a deputy sheriff, to your corporation at its last known address. The registered office may—but need not—have the same address as any of the corporation’s places of business. Under North Carolina law, the registered agent and the registered office must be continuously maintained in North Carolina.*

If service of process is not accomplished by serving the registered agent, it must satisfy the alternative requirements set out in Rule 4(j) (6), (7), or (8). For entities other than partnerships, this means serving one of the following:

- An officer of the company
- A director of the company
- A managing agent of the company

OR by leaving a copy in their office with a person apparently in charge of the office.

---

NOTE: GS 7A-217, which specifies specific rules for service of process in small claims actions, does not apply to artificial persons. The rules for serving them are set out in GS 1A-1, Rule 4.

## Special Rules & FAQs for Corporations & Similar Business Entities

- Corporations may represent themselves in small claims court and on appeal to district court..

In *Woods v. Billy's Automotive*, 174 N.C. App. 808 (2005), the appearance and participation at trial of the primary owner of Billy's Automotive Inc. was held to constitute a general appearance by the corporation and thus cure defects in service of process arising out of serving Billy—the owner—despite the fact that he was neither officer, director, or managing or registered agent!

- Corporations remain liable for their debts and the actions of their agents even if they are dissolved. GS Ch. 55 sets out a procedure by which creditors may assert claims against corporations even when the corporation is dissolved (whether voluntarily or administratively).

In the instance of known creditors, the corporation is required to notify them of the pending dissolution and the procedure and deadline for asserting claims. A creditor who receives notice and fails to assert a claim in a timely manner forfeits the right to collect on the debt. GS 55-14-06.

What if a creditor does not receive this notice or his properly-filed claim was never acted upon? What if the liability in question arose after the corporation was dissolved? GS 55-14-07 answers these questions. If a corporation publishes notice of its dissolution in accordance with the statute, claims not asserted within five years from date of publication are barred. GS 55-14-08 provides that undistributed corporate assets (including proceeds of insurance coverage relating to such claims) are available to pay claims against the dissolved corporation. In some situations, a claimant may be able to recover some portion of liquidated assets from a shareholder as well.

- There are two circumstances in which the law may hold individuals personally liable despite their efforts to avoid liability by incorporating their business.

**"Piercing the corporate veil"** is an equitable doctrine, similar to unconscionability. The presence of three elements supports application of the doctrine:

- Control by the defendant of the corporate entity to such an extent as to amount to the entity having no independent will or existence of its own; complete domination of not only finances, but also of policy and business practices;
- This control was used by defendant to commit fraud or wrong, to violate a statutory or positive duty, or a dishonest and unjust act;
- This control and breach of duty proximately caused the injury or unjust loss complained of.

Much like other equitable doctrines, piercing the corporate veil requires balancing concerns about fairness in the individual case against the value of having a predictable, consistent policy in service of the underlying overall goal—in this case, encouraging individuals to engage in commercial activity by insulating their homes, cars, and other personal assets from loss if the business fails or incurs other liability. The result of that balancing is that courts are reluctant to apply the doctrine in cases that are “close calls.” In deciding whether to impose liability, the following factors have been relied upon by the appellate courts:

- undercapitalization of the corporation
- non-compliance with corporate formalities
- complete dominion and control
- excessive fragmentation of a business into separate corporations without any reasonable justification therefor

The second legal theory that may result in individual liability for acts done in connection with corporate business springs from the familiar rule that **a person is responsible for their own negligent behavior.** In *White v. Collins Bldg Inc.*, 209 NC App. 48 (2011) the president and sole shareholder of Collins Building Inc. argued that he could not be held personally liable for negligence in supervising the construction of plaintiff’s home, since he was at all times acting on behalf of the corporation. The Court disagreed, saying that while the negligence of Mr. Collins might indeed be imputed to his corporation under the theory of *respondeat superior*, the fact that the corporation might be liable did not relieve him of personal liability for his own negligence. In a thoughtful opinion which discussed previous cases both from North Carolina and other states, Judge Stephens characterized this theory of liability as one of “the two most common methods of establishing personal liability in a business setting,” –with the other being piercing the corporate veil.

## Procedural Issues Related to Businesses

### Service of process

As we have seen already, some special rules govern service of process on artificial persons. For the most part, small claims magistrates are somewhat removed from ruling on whether there were errors in serving the defendant, because of GS 7A-221’s provision that objections to jurisdiction over the person (which is the essence of the argument that service of process was improper) be heard by a district court judge. The same statute also provides that the objection is waived if not made by motion or in the defendant’s answer prior to date of trial. Nevertheless, there are times when a magistrate, in ruling on another issue, must have some understanding of whether proper service was

accomplished. This typically comes up when it appears that plaintiff may not have properly named the defendant in the complaint and summons. See the discussion below, under *Amendments*.

## Venue

GS 7A-221 also provides that objections to venue must be made before trial or waived, but magistrates nevertheless must make this determination because of the limited authority of the chief district court judge to assign cases to small claims court under GS 7A-211 (requiring at least one defendant to be a resident of the county). Even if no objection is made by the defendant to venue, a magistrate who hears a case not meeting the residency requirement has no authority to enter judgment.

---

---

---

### *What is the residency of a corporation?*

A corporation either formed in North Carolina or formed elsewhere but maintaining a registered office in NC is a legal resident of the county in which its registered or principal office is located, or where it maintains a place of business. GS 1-79.

The registered office of a corporation is merely the business address of the registered agent.

The principal office of a corporation, according to the Secretary of State, is *the location where the business has its office or where the corporate records are kept if no such business office exists. If the corporation has a principal office upon creation, the Articles of Incorporation must identify the complete street address of that office, along with the county in which it is located. The articles of incorporation must also state the complete mailing address of the principal office if the mailing address is different from the street address. The annual report requires a principal office location. See also GS 55-1-40(17).*

If a corporation has no registered office, no principal office, and no place of business, its residence is any county in which it is regularly engaged in carrying on business.

## Motions to amend the summons and/or complaint

GS 1A-1 Rule 4 provides that the court may allow “any process or proof of service thereof to be amended” . . . “[a]t any time, before or after judgment,” on whatever terms or conditions the court finds is just “unless it clearly appears that material prejudice would result to substantial rights of the [defendant].”

GS 1A-1 Rule 15, Amended and Supplemental Pleadings, provides

- (a) *Amendments.* - A party may amend his pleading once as a matter of course at any time before a responsive pleading is served . . . . Otherwise a party may amend his pleading only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires. . . .

*(b) Amendments to conform to the evidence. - When issues not raised by the pleadings are tried by the express or implied consent of the parties, they shall be treated in all respects as if they had been raised in the pleadings. Such amendment of the pleadings as may be necessary to cause them to conform to the evidence and to raise these issues may be made upon motion of any party at any time, either before or after judgment, but failure so to amend does not affect the result of the trial of these issues. If evidence is objected to at the trial on the ground that it is not within the issues raised by the pleadings, the court may allow the pleadings to be amended and shall do so freely when the presentation of the merits of the action will be served thereby and the objecting party fails to satisfy the court that the admission of such evidence would prejudice him in maintaining his action or defense upon the merits. The court may grant a continuance to enable the objecting party to meet such evidence.*

Plaintiffs are allowed to change – “amend”—their complaints even after trial begins, so long as the defendant has adequate notice and time to prepare a response. A small change—such as correcting the spelling of a name—requires little notice, while a significant change, such as asking for money instead of personal property, may require a continuance. Amendments are NOT allowed if they change the party being sued; in that case, the plaintiff must file another lawsuit and serve the proper defendant. An amendment can literally be handwritten on the complaint, and should be noted in the judgment.

For cases involving corporations, the key to solving the puzzle presented by many of them is determining whether plaintiff (1) sued and served the correct defendant, using the wrong name, or (2) sued the wrong defendant.

## “What In the World is an LLC?” Worksheet

### What Can You Tell From an Annual Report?

Name of corporation: \_\_\_\_\_

Name of registered agent: \_\_\_\_\_

Location of registered office: \_\_\_\_\_

Names of principal officers: \_\_\_\_\_

Location of principal office: \_\_\_\_\_

### Applying Procedural Rules

In what county or counties may this corporation be sued in small claims court?

\_\_\_\_\_

Name the individuals authorized to accept service on behalf of this corporation:

\_\_\_\_\_