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When people start businesses, they tend to focus on visible pieces like finding customers, generating revenue, and getting something up and running quickly. Formation often becomes a box to check. An LLC gets created online in a matter of minutes, a filing confirmation comes back from the state, and the owners move on. That speed is appealing.

It’s also where many problems begin.

Forming a business entity isn’t just an administrative task. It’s the moment where liability protection, tax treatment, ownership rights, and business controls are set in motion. The documents created or forgotten at the outset often determine how later disputes are handled, who makes decisions, and what happens when circumstances change.

Why An Operating Agreement Matters

One of the most important and frequently overlooked documents is the *operating agreement*.

An operating agreement isn’t just paperwork; it’s the rulebook of how the business runs. It defines who owns what, who makes what decisions, how money is distributed, and what happens when things don’t go as planned. Without it, the business is operating under default state laws the owners likely know nothing about and wouldn’t have chosen. That distinction matters more than most business owners realize.

Operating agreements force owners to answer hard questions early when the business is still new, relationships are intact, and decisions can be made rationally instead of emotionally.

At a minimum, a well-drafted operating agreement should address:

- **Ownership percentages.** Who owns what and how ownership is measured.

- **Voting rights.** Whether control follows ownership or is structured differently. Equal ownership doesn't always mean equal control. In many cases, it shouldn't.
- **Management authority.** Who's responsible for day-to-day decisions versus major business actions.
- **Capital contributions.** Who's putting money into the business, when, and what happens if additional capital is needed later.
- **Profit and loss allocations.** How and when money is distributed, and whether distributions are tied strictly to ownership percentages.
- **Exit events.** What happens if an owner wants to leave, becomes disabled, goes through a divorce, or dies.
- **Transfer restrictions.** Whether an owner can sell or transfer their interest and to whom.
- **Buy-sell provisions.** How an ownership interest is valued and purchased when someone leaves.
- **Dispute resolution.** How disagreements are handled before turning into litigation.

None of these issues are theoretical. They're the points where businesses most often break down, and when they aren't addressed in advance, they result in uncertainty, conflict, and eventually, expense.

What Happens Without an Operating Agreement

Here's a common situation. Two friends form an LLC and agree to split everything 50/50. They trust each other, want to keep things simple, and skip the operating agreement entirely.

That works for a while because both friends are motivated. Decisions come easily, and money is either reinvested or not yet significant.

Time passes, and the business grows.

One owner begins working full-time in the business; the other remains less involved. The active owner expects to be paid more for their time and effort. The other disagrees, pointing to the 50/50 ownership. At the same time, decisions that took minutes early on now have real financial consequences. The owners begin to disagree on whether to expand, take on debt, or distribute profits.

Without an operating agreement, there's no clear answer to any of these questions. State default rules step in, often requiring equal voting power and offering no practical mechanism to break deadlocks. Neither owner can move forward without the other. Neither has a clear exit path. What started as a simple, low-cost formation becomes a

stalled business or a lawsuit.

These situations aren’t unusual. They’re all too predictable. This isn’t bad intent; it's a failure to define expectations at the outset.

Even a single-member LLC benefits from an operating agreement. Banks, investors, and courts often expect to see one, and it reinforces the separation between the owner and the business. This is *crucial* for maintaining liability protection.

An LLC Needs More Than Formation

The moral of the story is: Forming an entity is just the first step. Deciding how the entity functions determines whether it works.

An operating agreement is where that decision is made.