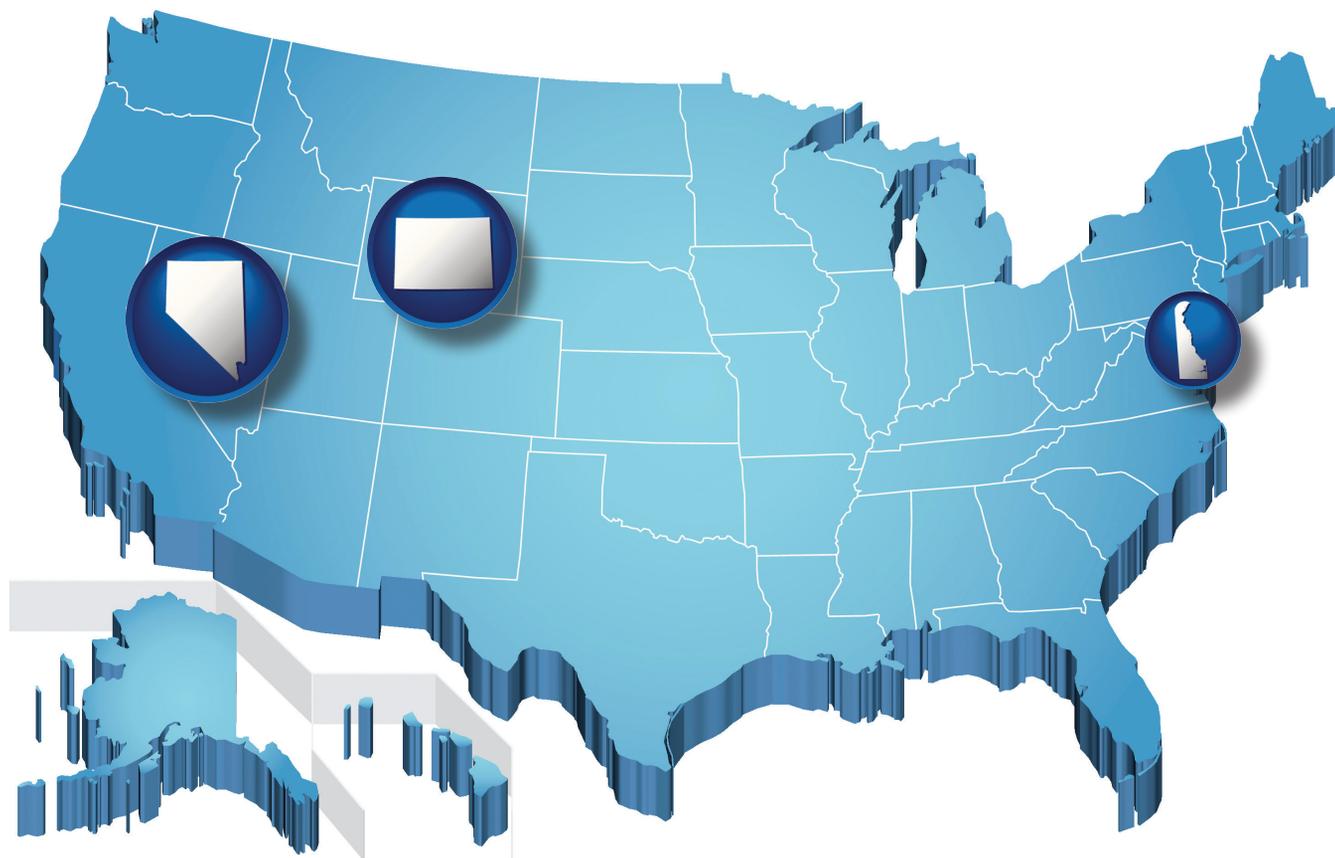


Long Island BusinessNEWS

MAY 15-21, 2015 | VOL. 62 | NO. 21 | \$2.00 | LIBN.COM



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STATE OF AFFAIRS

Should your business incorporate in Delaware, Nevada or Wyoming?

By **BERNADETTE STARZEE**

One of the first tough choices local entrepreneurs face when setting up a business is whether to incorporate in New York or a so-called corporate-friendly state.

Delaware – the corporate home of many of the Fortune 500 companies – is the granddaddy of such states, while Nevada and Wyoming have emerged as alternatives.

But while there are many good reasons to set up a corporation out of state, “none of those reasons has much to do with most startups,” said Alon Kapen, a partner in charge of the emerging companies and venture capital practice group at Uniondale-based law firm Farrell Fritz.

“Sites on the Internet steer businesses to incorporate in Delaware or Nevada, but

there’s no reason to organize in a state like that unless the business is looking to raise funds from venture capitalists or other investors right off the bat – which is unusual,” Kapen said.

When companies are seeking to raise capital or go public, “being a Delaware corporation or LLC [limited liability corporation] tends to enhance their prestige and credibility,” said Fred Skolnik, a partner in the corporate/securities law practice group at Certilman Balin Adler & Hyman in East Meadow.

Delaware is the “clear preference” among venture capitalists and underwriters, Kapen said, because of its “very well-developed body of corporate law.”

Delaware has “over 200 years of

well-developed case law, which provides for predictability” of what Delaware corporations can and cannot do, said William Gartland, a partner in the corporate business group at Lazer Aptheker Rosella & Yedid in Melville.

The state has a specialized Court of Chancery, in which judges, rather than juries, decide corporate cases – leading to more predictable results than jury trials, Kapen said.

“The Delaware courts have seasoned judges who really understand the nuances of corporate law,” Kapen said.

In recent years, Nevada has tried to become the Delaware of the West, modeling its court system after the First State, Skolnik said.

“Nevada has become a hot state in connection with estate planning and asset protection matters,” said Ralph Rosella, managing partner at Lazer Apthecker Rosella & Yedid, noting people who want to preserve their wealth may set up non-operating entities there. “It’s harder for creditors who have judgments against the owners to reach assets in Nevada corporations.”

Nevada may also be advantageous for companies who are doing a reverse stock split, Skolnik said. In a reverse stock split, the company decreases the number of shares available in order to raise the price of each share.

“There’s more flexibility in Nevada in accomplishing this without having to go to the shareholders,” Skolnik said.

Wyoming has recently become aggressive in attracting corporations, with low organization fees and annual filing fees, but its laws are not as well-developed, Gartland said.

It’s relatively rare for New York companies to incorporate in Nevada or Wyoming.

“When clients have an intention of going public, we would most likely advise them to choose Delaware,” Gartland said.

“It’s most advantageous to publicly held companies due in large part to its favorable treatment of businesses.” Further, the financial community is very comfortable dealing with Delaware.

But for many startups, attorneys say there’s no place like their home state.

Pros and cons of incorporating in Delaware

“If you form XYZ Corp. in Delaware, and all you’re doing is opening a bagel store on Long Island – or several bagel stores on Long Island – it’s a waste of money,” said David Heymann, a partner in the corporate law practice group at Meltzer, Lippe, Goldstein & Breitstone in Mineola.



Photo by Bob Giglione

ALON KAPEN: For most LI startups, New York is the place to incorporate.

In addition to having to pay fees to set up the corporation, annual refiling fees and franchise taxes in Delaware, companies will have to file to do business in New York as a foreign entity (from another state).

“All you’re doing is double-paying for registration fees, and there’s no reason to be in Delaware – or Wyoming or Nevada or any other state that people think it’s great to be in,” Heymann said. “If you’re a single-state operator and you’re going to be closely held – if just you and a couple of your friends are going to own the business – you’re better off forming your entity in the state where you’re doing business.”

Companies don’t avoid paying high New York taxes by incorporating in another state because they are taxed in the state where they do business and generate revenue.

In 2008, New York State reformed certain laws to make it a more attractive place to incorporate, Kapen said.

For instance, corporations formed in New York before these amendments needed the consent of the stockholders holding two-thirds of outstanding shares to approve a merger. Now, only a simple majority – a much easier threshold – is needed, Kapen said.

Under the new rules, New York only requires that startups have one director and one officer. This is important, Kapen said, because it’s “difficult for startups to recruit directors and build a big management team.”

“New York has become more in-line with Delaware in that it’s much more management friendly in ways that are important to startups,” Kapen said.

When companies advance in their life-cycle and are looking to raise capital or go public, they may have to head south on I-95. In fact, when companies do a public offering, the underwriter will likely insist they incorporate in Delaware if they aren’t there already.

But there’s no reason to rush out of state.

“As your business grows, and you find you need to be in Delaware, you can reincorporate at that time,” Kapen said. “It’s not that disruptive; people do it all the time.”

In the meantime, such companies can avoid hassle and additional expenses in their initial years by incorporating in the Empire State.

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