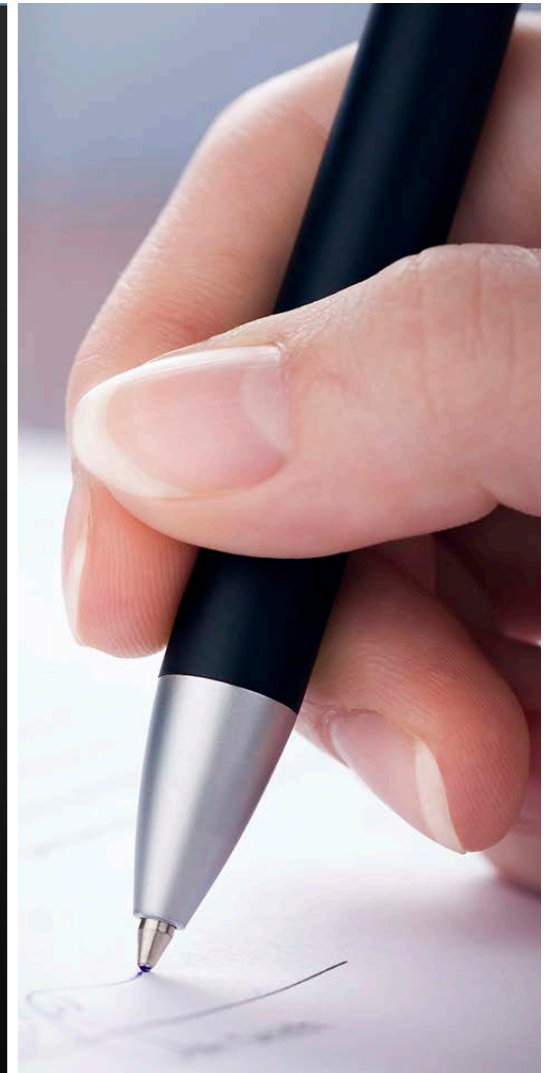


GUIDE TO SELECTING  
YOUR **SMALL BUSINESS**  
**LEGAL STRUCTURE**



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# INTRODUCTION

## FOUR BASIC STRUCTURE TYPES

- Sole Proprietorship
- Partnership — General and Limited
- Corporation — S Corporation, C Corporation
- Limited Liability Company (LLC)



# OVERVIEW OF LEGAL STRUCTURES – SOLE PROPRIETORSHIP

**SIMPLE**

**ONE OWNER**

**NOT LEGALLY SEPARATED FROM OWNER**

**LEGAL BUSINESS NAME SAME AS OWNER'S**

**EASY CASH WITHDRAWALS**

**QUARTERLY ESTIMATED TAX PAYMENTS**

**LICENSE OR PERMIT REQUIRED IN SOME  
STATES/MUNICIPALITIES**

# OVERVIEW OF LEGAL STRUCTURES – PARTNERSHIP

## **GENERAL PARTNERSHIP**

- Not separate from owners
- TWO or more owners
- Easy cash withdrawals
- Quarterly tax payments by individual owners
- Registered with state

## **LIMITED PARTNERSHIP**

- Limited liability partnerships (LLPs)
- Limits owners' liability
- Rules for profit/loss percentages; business decisions; addition and withdrawal of a partner and terms of operation

# OVERVIEW OF LEGAL STRUCTURES – C CORPORATION

**LEGALLY SEPARATE FROM OWNERS**

**ARTICLES OF INCORPORATION**

**ANNUAL FILINGS AND FEES TO STATE**

**SEPARATE CORPORATE BANK  
ACCOUNTS AND RECORDS**

**LIMITED CASH WITHDRAWALS**

**FEDERAL, STATE AND, IN SOME  
CASES, LOCAL TAXES**

**TAX ID NUMBER**

**INCOME TAX ON PROFITS**



# OVERVIEW OF LEGAL STRUCTURES – S CORPORATION

**SUBCHAPTER S DESIGNATION FROM IRS  
CHARTERED AS CORPORATION**

**PROFITS AND LOSSES PASS THROUGH TO SHAREHOLDERS  
PERSONAL TAX RETURNS**

**LOSSES LIMITED TO THE SHAREHOLDER'S TAX BASIS**

**SHAREHOLDERS PAID WAGES, DISTRIBUTIONS  
OF PROFITS OR COMBINATION**

# OVERVIEW OF LEGAL STRUCTURES – LIMITED LIABILITY COMPANY (LLC)

**HYBRID — LIMITED LIABILITY FEATURES OF CORPORATION  
AND TAX, OPERATIONAL FEATURES OF PARTNERSHIP**

**CALLS OWNERS “MEMBERS”**

**CONSISTS OF INDIVIDUAL, TWO OR  
MORE INDIVIDUALS, CORPORATIONS  
OR OTHER LLCs**

**PROFITS AND LOSSES “PASSED  
THROUGH” TO EACH MEMBER**

**MEMBERS REPORT PROFIT & LOSS  
LIKE OWNERS OF PARTNERSHIP**





# OPERATION AND CONTROL

ENTITIES	BASIC OVERVIEW
<b>Sole Proprietor</b>	<ul style="list-style-type: none"> <li>• Controlled by one person</li> </ul>
<b>Partnership — General</b>	<ul style="list-style-type: none"> <li>• Equal management rights and control, if not otherwise specified</li> <li>• Option to specify responsibilities and control in partnership agreement</li> </ul>
<b>Partnership — Limited</b>	<ul style="list-style-type: none"> <li>• Management and control by general partners</li> </ul>
<b>Corporation — C and S</b>	<ul style="list-style-type: none"> <li>• Governance established by bylaws</li> <li>• Shareholders approve articles of incorporation, mergers and dissolution of the company and elect directors</li> <li>• Directors responsible for major decisions, including selection of company officers</li> </ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"> <li>• Single-member like sole proprietorship</li> <li>• Multi-member like limited partnership</li> </ul>

# INVESTMENT

ENTITIES	BASIC OVERVIEW
<b>Sole Proprietor</b>	<ul style="list-style-type: none"><li>• No outside investments</li></ul>
<b>Partnership — General</b>	<ul style="list-style-type: none"><li>• Equal ownership of assets and liabilities unless otherwise defined</li></ul>
<b>Partnership — Limited</b>	<ul style="list-style-type: none"><li>• Ownership percentages vary</li><li>• Set procedures for intake and departure of partners</li></ul>
<b>Corporation — S</b>	<ul style="list-style-type: none"><li>• One class of stock to up to 100 shareholders</li></ul>
<b>Corporation — C</b>	<ul style="list-style-type: none"><li>• Multiple classes of stock and bonds</li></ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"><li>• Like sole proprietorship for single-member LLCs</li><li>• Like partnership for multiple-member LLCs</li></ul>

# CONTINUITY AND TRANSFERABILITY

ENTITIES	BASIC OVERVIEW
<b>Sole Proprietor</b>	<ul style="list-style-type: none"><li>• Continues until abandoned or death of owner</li><li>• Freely transferred by selling all or a portion of assets</li></ul>
<b>Partnership — General and Limited</b>	<ul style="list-style-type: none"><li>• Dissolves if a general partner dies or leaves, unless agreement provides for continuation by remaining partners</li></ul>
<b>Corporation — C and S</b>	<ul style="list-style-type: none"><li>• Exists in perpetuity</li><li>• Ownership transferred by sale or inheritance of stock</li></ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"><li>• Determined by organizing and operating documents</li></ul>

# LEGAL LIABILITY

ENTITIES	BASIC OVERVIEW
<b>Sole Proprietor</b>	<ul style="list-style-type: none"><li>• Unlimited personal liability</li></ul>
<b>Partnership — General and Limited</b>	<ul style="list-style-type: none"><li>• General partners fully liable</li><li>• Limited partners responsible to the extent of investment</li></ul>
<b>Corporation — C and S</b>	<ul style="list-style-type: none"><li>• Shareholders liable to the extent of investment</li><li>• Management incurs some personal liability</li></ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"><li>• Similar to corporate shareholders</li><li>• Members not liable for debts and liabilities</li><li>• Management incurs some personal liability</li></ul>

# COMPENSATION AND PAYROLL TAXES

ENTITIES	BASIC OVERVIEW
<b>Sole Proprietor</b>	<ul style="list-style-type: none"> <li>• Pays quarterly self-employment taxes</li> </ul>
<b>Partnership — General</b>	<ul style="list-style-type: none"> <li>• Each partner pays quarterly self-employment taxes on share of income</li> </ul>
<b>Partnership — Limited</b>	<ul style="list-style-type: none"> <li>• Each general partner pays quarterly self-employment taxes on share of income</li> <li>• Limited partners not subject to self-employment taxes</li> </ul>
<b>Corporation — C and S</b>	<ul style="list-style-type: none"> <li>• Income, Social Security and Medicare taxes withheld from wages paid to shareholder employees</li> </ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"> <li>• Varies according to tax treatment</li> <li>• Inactive members not subject to self-employment taxes</li> </ul>

# BUSINESS STRUCTURE PROS AND CONS

ENTITIES	PROs	CONs
<b>Sole Proprietor</b>	<ul style="list-style-type: none"> <li>• Inexpensive and simple</li> <li>• One level of tax</li> <li>• No separate tax return</li> </ul>	<ul style="list-style-type: none"> <li>• Unlimited personal liability</li> <li>• Ownership limited to one person</li> </ul>
<b>Partnership</b>	<ul style="list-style-type: none"> <li>• Ownership not limited to one person</li> <li>• One level of tax on net income</li> <li>• Income and expenses allocation can be unrelated to percentage of ownership</li> </ul>	<ul style="list-style-type: none"> <li>• Unlimited personal liability</li> <li>• Responsible for business actions of other partners</li> <li>• Requires separate tax returns</li> </ul>
<b>S Corporation</b>	<ul style="list-style-type: none"> <li>• Limited personal liability for shareholders</li> <li>• Business net income taxed as personal income of shareholders</li> </ul>	<ul style="list-style-type: none"> <li>• Requires separate tax returns</li> <li>• Restrictions on adding investors</li> <li>• Net income allocated according to percentage of ownership</li> </ul>
<b>C Corporation</b>	<ul style="list-style-type: none"> <li>• Limited personal liability for shareholders</li> <li>• Easy to transfer ownership/add investors</li> <li>• Perpetual continuity presumed</li> </ul>	<ul style="list-style-type: none"> <li>• Requires separate tax returns</li> <li>• Net income may be double taxed</li> <li>• More costly to set up and maintain</li> </ul>
<b>Limited Liability Company (LLC)</b>	<ul style="list-style-type: none"> <li>• Limited personal liability for members</li> <li>• Income and expenses can be allocated in a manner unrelated to percentage of ownership</li> </ul>	<ul style="list-style-type: none"> <li>• Not automatically perpetual like S or C corps</li> <li>• Cost to set up and maintain</li> </ul>

# HOW A CPA CAN HELP

**EXPERT ANALYSIS AND RECOMMENDATIONS**

**REFERRALS**

**BOOKKEEPING AND TAX SERVICES**

**PREPARATION OF PERIODIC  
FINANCIAL STATEMENTS**

**FINANCIAL STATEMENT  
REVIEW OR AUDIT**

