BUSINESS STRUCTURES- WHAT WORKS FOR YOU

- First decision for a business owner:
  - How will the business be structured.
  - All businesses must adopt some legal configuration.
  - How the business is owned, who is in control, personal liability, life span, and financial structure.
  - May want to ask your attorney and accountant to assist in the selection.

  - Note: sole proprietorship is not always regarded as having a legal configuration.

- Considerations
  - Level of control
  - Level of structure you are willing to accept-requirements of ownership.
  - Business’s vulnerability to lawsuits
  - Tax implications associated with the business form
  - Re-investment of earnings into the business
  - Access to income for you from the business.
  - Succession of the business

- 5 Business Structures commonly utilized
    - 1. Sole proprietorship
    - 2. Partnerships
        - Limited Liability
        - Limited Liability Limited
        - General

- 3. Limited Liability Company
- 4. Subchapter S Corporation
- 5. C Corporations (referred as a capitalized corporation) are not addressed in this presentation.

- The advantages and disadvantages of each form of business structure:
  - 1. Sole Proprietorship—advantages
    - Vast majorities of small business chose this form initially.
    - Owner owns all the assets and profits generated and makes all the decisions
    - Also assumes all of its liabilities and debts
    - Easy to form to organize—no required ownership meetings, board of directors, etc.
    - Offers complete control of the business including your business name which is different than your name
    - Profits from business flow directly to owner's tax return including self employment taxes
    - Easiest form of business to dissolve

- 1. Sole Proprietorship—Disadvantages:
  - Owner has unlimited liability and is responsible for all the debt against the business.
  - May have difficulties raising funds for the business and not ideal for high risk businesses
  - Hiring qualified employees particularly those interested in owning part of the business.
  - May limit certain taxable deductions such as medical insurance premiums

- 2. Partnerships
  - General

PARTNERSHIP

- 2 or more people share ownership of a business.
- Law does not distinguish between the business and its owners.
- Partnership agreement includes:
  - How decisions are made.
  - How profits are shared.
  - How to resolve disputes.
  - How future partners can be added to the business.
  - How partners can be bought out.
  - How to dissolve the partnership.
  - How much time and capital each partner will contribute.

PARTNERSHIP

- Advantages:
  - Relatively easy to establish.
  - May be able to raise additional capital with additional partners.
  - Profits are pass through.
  - Could be incentives for employees if they can buy at come point.
  - Business may have a complementary relationship between partners.
  - Possible income tax advantages over sole proprietorship.

PARTNERSHIP

- Disadvantages:
  - Partners are jointly and individually liable.
  - Profits are shared.
  - Partners cannot receive a salary.
  - Some tax implications impact the business as well as owners.
  - Disagreements can occur.
  - Some employee benefits may not be deductible.
  - Partnership may have a defined life (withdrawal or death of a partners).

TYPES OF PARTNERSHIPS

1. General-partners are equally responsible for management, liability, share of profits or losses based on their partnership agreement.
2. Limited Partnership and Partnership with Limited liability

   -Limited means most of partners have limited liability (investment) and limited input regarding management.

   -Is more complex and formal than a general partnership

TYPES OF PARTNERSHIPS

Joint Venture

- Acts as a general partnership but is generally organized for a shorter period or single project.
- If joint venture repeats the activity may be recognized as an on-going partnership and will file tax returns as a partnership.
- May be used in conjunction with sole proprietorship for income tax purposes.

CORPORATIONS

- Are chartered in state where the business is head quartered.
- Are considered by law to be a unique entity separate and apart from the owners.
- Can be taxed, sued, and can enter into contracts
- Owners are the shareholders.
- Shareholders must elect a board of directors (oversees the operation).
- Have a life of its own-does not dissolve when ownership changes

CORPORATIONS

- Advantages
  - Shareholders have limited liability (debt or judgments).
  - Generally shareholders are only liable for up to their capital contribution. (Officers can be held personally liable for their actions such as failure to withhold and pay employment taxes.)
  - Can raise funds through sale of stock.
  - May deduct cost of benefits and salaries paid.
  - Can elect S Corporation status if certain requirements are met. (This election enables firm to be taxed much like a partnership.)

CORPORATIONS

- Disadvantages
  - More time and money to incorporate.
  - May be monitored by federal, state agencies. (more paperwork)
  - Could result in higher overall taxes. (Recent tax bill reduced tax to 21 percent.)
  - Dividends paid are not deductible from business income. (Income could be taxed twice.)
  - Required to have regular ownership meetings, ownership of shares=voting power.

CORPORATIONS

- Subchapter S
  - A tax election only.
  - Enables shareholder to treat earnings and profits as distributions.
  - Passes directly to personal tax return.

LIMITED LIABILITY COMPANY

- Relatively new hybrid business structure. Not recognized by IRS as a legal structure.
- Designed to provide limited liability features of a corporation and tax efficiencies and operational flexibility of a partnership.
- Can be taxed, sued, and can enter into contracts.
- Formation is more complex than general partnership.
- Owners are members. (could be a single owner.)
- Duration is usually determined when organizational papers are filed.
- Time limit ban be continued if desired by the members.

LIMITED LIABILITY COMPANY

- LLC must not have more that two of four characteristics which define a corporation..
  - Limited liability to the extent of assets in the business.
  - Continuity of the life of the LLC.
  - Centralization of management
  - Free transfer of ownership interests.
- Taxed as a partnership mostly.

SOURCE: info@KCSourceLink