U.S. LEGAL BUSINESS FORMS

Know the differences & types of various business entities

SOLE PROPRIETORSHIP

The easiest and simplest business structure, a sole proprietorship is an unincorporated business owned and run by one person with no distinction between the business and individual. Examples: Plumbers, Repairmen, Housecleaners

TAXES: A sole proprietor reports income and/or losses and expenses by filing a Schedule D, along with standard Form 1040. Then the "bottom-line amount" from Schedule C is transferred to his/her personal tax return.

FORMATION: Business activity done as an individual makes you a sole proprietor. However, there are Licenses, Permits and Registrations necessary to run the business. You may also choose to run a sole proprietorship under a Fictitious Trade name or DBA (Doing Business As).

ADVANTAGES:
-Very easy and inexpensive to create with low overhead costs
-Complete control over the business
-Lowest tax rates

DISADVANTAGES:
-Personally liable for business debts and obligations
-Difficulty in raising capital due to lack of repayment credibility
-Limited life, business literally dies with you

PARTNERSHIP

A partnership is a business wherein 2 or more people share ownership, and each contributes financial resources, property, labor, and skill, as well as shares profits and losses of the business.
Examples: Hewlett Packard, Chanel, Microsoft

TAXES: Partnerships file an annual income return to report the finances of the business, but each partner is responsible for handling taxes for their respective share of income/loss.

FORMATION: The business must be registered with the state and file appropriate Licenses, Permits and Registrations. There are 3 types of partnerships:
1) General Partnership: divide profits, liability and management duties equally
2) Limited Partnership: grant limited liability and input to partners dependent on that partner's investment
3) Joint Ventures: act as a general partnership for a limited time

ADVANTAGES:
-Simple and inexpensive to form
-Ease of capital acquisition due to shared financial commitment
-Each partner contributes an ideally unique skill set
-Unique ability to offer employees the incentive of becoming a partner

DISADVANTAGES:
-Personally liable not only for actions, debts and obligations of the business but also for other partners
-Personal disagreements between partners can cause problems
-Partners share profit and success with each other even if some aren't pulling their weight

LLC - LIMITED LIABILITY CORPORATION

A limited liability company (LLC) offers the liability of a corporation with structure a lot like a partnership with the members of the LLC being the "owners."
Examples: YouTube, Kaiser Permanente, United States Postal Service, Chrysler Group LLC

TAXES: Under partnership tax treatment, each member of the LLC reports income or loss on his or her individual tax return. However, an LLC with either single or multiple members may elect to be taxed as a corporation through filing IRS Form 8832.

FORMATION: Documents that must be filed include: Articles of Organization, an Operating Agreement, Licenses, Permits and Registrations. Additionally, the name of an LLC must be unique, indicate that it is an LLC and not include restricted words.

ADVANTAGES:
-Better chance of raising capital, similar to a partnership
-Limited liability benefits as liability cannot exceed amount invested in the company
-Fewer restrictions on sharing profits among LLC members
-Less registration paperwork, smaller start-up costs and ease of operation as compared to a Corporation

DISADVANTAGES:
-In some states, if a member leaves an LLC, it can dissolve the business and force participating members to fulfill obligations
-The Net Income of an LLC is subject to self-employment taxes
-Investors may be more comfortable investing funds in the better-understood corporate form with a view toward an eventual IPO

S CORPORATION

The IRS will designate some corporations as an S Corporation to allow them to avoid double taxation (once to the corporation and again to the shareholders). Examples: DELL, PriceWaterHouseCoopers, Fidelity Investments

TAXES: Filing as an S Corporation lets you enjoy the limited liability of a corporate shareholder but pay some income taxes as if you were a sole proprietor or partner (distributions are taxed differently).

FORMATION: You must first create a regular LLC or corporation by filing either Articles of Organization or Articles of Incorporation with your secretary of state's office. Then, to be treated as an S Corporation, all shareholders must sign and file IRS form 2553.

ADVANTAGES:
-Employment tax is limited only to the wages of an employed shareholder
-There are some tax credits available as business expenses
-The company is separate from the shareholders, allowing them to sell shares without impacting the business

DISADVANTAGES:
-Stricter operational process than a Partnership or regular LLC
-Shareholders working for the business must be paid fair market value compensation or the IRS can reclassify corporate earnings as wages for taxation purposes
-There cannot be more than 100 shareholders
-Foreign share ownership is prohibited

C CORPORATION

Corporations, or C Corporations, are an independent legal entity owned by shareholders. The business itself is legally liable for actions and debts rather than the shareholders.
Examples: AT&T, Boeing, GE, ExxonMobil, Johnson & Johnson

TAXES: Corporations pay income tax on their profit, sometimes twice (once on company profit, second on the dividends paid to the shareholders).

FORMATION: Aside from the other minimum business requirements, the business must file Articles of Incorporation. The corporation is generally required to include a corporate designation in its name.

ADVANTAGES:
-The ability to offer an Initial Public Offering (IPO) to raise capital
-Shareholders' personal assets are protected due to limited liability
-Corporations can file taxes separately from shareholders
-Can be enticing to high-quality employee due to competitive benefits and stock ownership

DISADVANTAGES:
-Tax laws and legal requirements are complex
-High organizational and operational costs
-Corporations are subject to double taxation

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