

CHOICE OF ENTITY

THE TAX DECISION

Clare G. Cole CPA

Adapted by MA Small Business
Development Center

WHAT ARE THE CHOICES?

- Sole proprietorship
- Partnership
- Corporation
- Limited liability company or LLP

KEY BUSINESS ISSUES

- OPERATIONS
- HOLDING ASSETS
- STAYING SMALL
- GOING PUBLIC
- ACCESSING CAPITAL

KEY DIFFERENTIATORS

- PERSONAL LIABILITY PROTECTION
- TAX ADVANTAGES
- COST
- SIMPLICITY

SOLE PROPRIETORSHIP

- ADVANTAGES
 1. SIMPLE, NO SEPARATE FILING
 2. NO STATE FILINGS
 3. LOSSES PASS THROUGH

SOLE PROPRIETORSHIP

- DISADVANTAGES
 1. PERSONAL LIABILITY
 2. LIMITED ACCESS TO CAPITAL
 3. SELF EMPLOYMENT TAX

GENERAL PARTNERSHIP

- **ADVANTAGES**
 1. **SINGLE LEVEL OF TAXATION**
 2. **LOSSES PASS THROUGH**
 3. **SIMPLE ADMINISTRATION**

GENERAL PARTNERSHIP

- DISADVANTAGES
 1. PERSONAL LIABILITY
 2. LIABILITY FOR PARTNER'S COMMITMENTS
 3. LIMITED ACCESS TO CAPITAL

CORPORATION

- **ADVANTAGES**
 1. LIMITED LIABILITY
 2. ACCESS TO CAPITAL
 3. OWNER BENEFITS DEDUCTIBLE
 4. LESS PAYROLL TAXES

CORPORATION

- DISADVANTAGES
 1. DOUBLE LAYER OF TAXATION
 2. TAX ON EXCESS RETAINED EARNINGS
 3. PRORATA EARNINGS DISTRIBUTION
 4. MORE ADMINISTRATION
 5. STATE FILINGS REQUIRED

SUBCHAPTER “S” CORPORATION

- ADVANTAGES
 1. ONE LEVEL OF TAX
 2. LIMITED LIABILITY
 3. LESS PAYROLL TAXES
 4. LOSSES PASS THROUGH (UP TO ‘BASIS’)

SUBCHAPTER “S” CORPORATION

- DISADVANTAGES
 1. LOTS OF RULES
 2. ONE CLASS OF OWNERSHIP
 3. NEED “BASIS” FOR LOSSES
 4. PRORATA DISTRIBUTIONS
 5. LIMITED ACCESS TO CAPITAL
 6. STATE FILINGS REQUIRED

LIMITED LIABILITY COMPANY LLC

LIMITED LIABILITY PARTNERSHIP LLP

- **ADVANTAGES**
 1. SINGLE LEVEL OF TAXATION
 2. LOSSES PASS THROUGH
 3. LIMITED LIABILITY
 4. ADMINISTRATION BY AGREEMENT
 5. BROADER OWNERSHIP ALLOWED

LIMITED LIABILITY COMPANY LLC

LIMITED LIABILITY PARTNERSHIP LLP

- DISADVANTAGES

- SELF EMPLOYMENT TAX
- NEW TYPE ENTITY, NOT MUCH CASE LAW
- STATE FILINGS REQUIREMENTS

WHICH TO CHOOSE?

- SOLE PROPRIETORSHIP OR GENERAL PARTNERSHIP
 1. LITTLE CAPITAL REQUIRED
 2. NO LIABILITY PROTECTION REQUIRED
 3. LIMITED ASSETS AT RISK
 4. NO SALE OF BUSINESS ANTICIPATED

WHICH TO CHOOSE?

- “C” CORPORATION
 1. LIMITED LIABILITY DESIRABLE
 2. PASS THROUGH INCOME IS NOT DESIRED
 3. LARGE GROWTH ANTICIPATED
 4. BROAD OWNERSHIP DESIRED
 5. BROAD ACCES TO CAPITAL DESIRED
 6. FUTURE SALE OF BUSINESS POSSIBLE

WHICH TO CHOOSE?

- “S” CORPORATION WHERE:
 1. BUSINESS WILL REMAIN RELATIVELY SMALL
 2. CAPITAL IS RETAINED FOR GROWTH
 3. NO SIGNIFICANT INVESTMENT IN APPRECIABLE ASSETS
 4. LIMITED LIABILITY DESIRABLE
 5. NO SPECIAL OWNERSHIP REQUIRED
 6. SINGLE LEVEL OF TAXATION

WHICH TO CHOOSE?

- LIMITED LIABILITY COMPANY
 1. LIMITED LIABILITY IS DESIRABLE
 2. HOLDS APPRECIABLE ASSETS
 3. SPECIAL OWNERSHIP REQUIREMENTS
 4. PASSIVE ACTIVITY
 5. DISPROPORTIONATE DISTRIBUTION