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WHAT'S THE DIFFERENCE?

Introduction

In the recent past, choosing a business entity under which to operate was easy. Either businesses operated as a sole proprietorship, a partnership, and S Corporation or they incorporated as a C Corporation. There were clear advantages and disadvantages to each one. The sole proprietorship and partnership had the advantage of simplicity and lack of formal arrangements. The C Corporation was for national companies, and the S Corporation was for those individuals needing asset protection and a formal entity in which to operate in.

Today the business structure is not a default arrangement. Business people have an alphabet soup of business types to choose from. Though many of the new forms offer limited liability and single layer taxation, the tax and legal differences are not nearly as clear as they used to be in the past. This article will discuss three types of business entities and point out some very subtle and not widely known differences between the chosen entities. All three entities are excellent for any small business person to operate a business.

When deciding which entity to operate under, the business owner must take into consideration legal liability, tax circumstances while operating and dissolution, the person's goals, and the size of the operation among other factors. Tax circumstances are of utmost importance when choosing an entity. However, ease of transferability, legal protection, and other factors are affected under each entity type. The advantages of having a Limited Liability Company (LLC), S Corporation, and C Corporation are discussed below.

The Limited Liability Company

With an LLC, there are no restrictions on ownership. An S Corporation, on the other hand, does have restrictions on ownership. To hold an S Corporation status, one must be a resident and citizen of this country. No more than 100 people are allowed to own stock. If the ownership requirements are violated, the company losses its S Corporation status and it can not attain S Corporation status for a number of years.

With an LLC, these restrictions do not exist and its status is not jeopardized. While most LLCs will maintain membership of well under 100 members, the option or ability to expand the number of investors rapidly does exist. Many immigrants just starting business can benefit from this form of business as well without suffering from double taxation.

There are fewer formalities in maintaining an LLC. This is a major convenience and aides in limiting liability. The types of businesses identified here are all subject to being disregarded as an entity if the owner does not obey formalities. This is what is known as "veil piercing" and it happens when company owners do not observe formalities in paperwork, meetings, and otherwise use the business as an "alter ego".

While the owner of the business can not use the company as an alter ego to defraud people out of money, the LLC does not require the formalities that corporations do. Hence the LLC can be a better insulator against liability if maintenance of meetings and documents is going to be an issue.

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