

Legal Structures Matrix

Legal Entity	Ownership	Liability	Tax	Management	Expense and formality	Tips
Sole Proprietorship	Individual	Owner has unlimited personal liability for business debts/obligations.	Owner reports profits/losses on his/her personal tax return, using Schedule C to Form 1040 (or Sch C-EZ).	Owner has 100% control in decision-making	Simple and inexpensive to create and operate; no filing required but if business name is different than owner's name, then register assumed business name with state.	Open a business checking account separate from your personal bank account.
Limited Liability Company	Member(s) Ownership is expressed in 1) # of units, or 2) % of ownership interest, as written in an Operating Agreement.	Similar to corporations in that owners have limited personal liability for the debts and actions of the LLC.	LLC with 2 or more members can choose to be taxed as a 1) partnership (pass-through taxes paid by members) or 2) a corporation. LLC with <u>single</u> member can elect to be taxed 1) as a corporation or 2) <u>disregarded</u> as an entity separate from its owner. In this case, profits/losses pass through directly to the single member.	Must elect to be 1) manger-managed or 2) member- managed. If manager-managed, Members elect one or more managers.	LLCs with 2 or more members should work with an attorney to create an operating agreement. An Operating Agreement sets forth who manages, conditions for new members to join, tax allocation, etc.	If you expect to have employees, strongly consider obtaining a separate EIN (Federal Employer Tax Identification Number) from the IRS. No state requirement to hold annual meetings of members or managers. Cannot offer stock ownership to employees.
Corporation	Shareholder(s). Shareholders own stock in a corporation	Limited liability for shareholders, officers, directors Shareholder liability is limited to his/her investment	Entity est. 35% Distributions to shareholders Separate taxable entity. Owners pay taxes on salaries, bonuses, and dividends.	Shareholders annually elect directors. Directors elect officers to management daily operations.	More expensive to create; annual meetings and disclosure formalities	Well understood structure for when you seek external financing. One person can be a corporation's shareholder, president, and secretary. Annual meetings required by state statute

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S-Corporation	Shareholder(s)	Shareholders have limited liability	Profit/losses are reported on owners' personal tax returns	Officers elected by directors. Directors elected by shareholders.	Same formalities as corporation	Can only have 1 class of stock. Max of 100 shareholders who must be individuals or certain estates/trusts
General Partnership	An association of 2 or more people in business. Partners own % of interest in the business	Unlimited person liability Partner is liable for her own actions, the actions of other partners and for employees.	Tax-reporting entity (Form 1065) but not tax-paying entity. Profits/losses are allocated equally to partners, unless an agreement says otherwise.	Partners have equal voting rights, Unless stated in a partnership agreement. Typically, shared management	Simple and inexpensive to create and operate; If name is different than partners, register name with the state	Have an agreement that explains management responsibilities, transfer of partnership interests, and what happens in the case of disagreement. This structure is not common anymore. Wise to choose any other structure but this one.
Limited Partnership	Partners own % of interest in the business. Consists of a General Partner and one or more limited partners.	General Partner – unlimited Limited Partner – limited to amount of investment as long as don't participate in management.	Normally, tax is passed –through to partners if certain conditions are met. Otherwise, taxed as corporation Absent agreement, profits/losses are allocated based on contribution of the partner	General Partner	More expensive than forming a General Partnership. Must file with state	Most suitable for companies that invest in real estate
Nonprofit a) Public Benefit b) Mutual Benefit	No owners	Organization's assets	No federal/state tax payments required if correctly filed and maintain tax exempt status.	Board of Directors (min. of 3) If entity has members, they have participation rights	Annual actions are taken by the Board and members, similar to a corporation	Transactions between nonprofit and insiders (i.e. directors) are tricky. Stay current on all filings with the government.

If your business involves risk, you want to choose a legal structure that offers some liability protection for your personal assets.

Federal Corporation Income Tax Rates for 2010, 2009 are lower than for most individuals up to \$50,000.

Up to \$50,000 = 15%, \$50,000-\$75,000 = 25%, \$75,000-100,000 = 34%; \$50,000 for individual is taxed between 15% and 25%