Fact Sheet

Limited Liabilities and Corporations

Limited Liability Companies (LLC):

> Definition: a flexible form of business ownership blending several features of corporation and partnership structures.

An LLC is **<u>not</u>** a corporation or partnership. The primary characteristics that are shared between a LLC, corporation and a partnership are:

1. A corporation **is** limited liability.
2. A partnership **also has the availability of** pass- through income taxation.

A LLC is more flexible than a corporation and its well suited for companies with a single owner. Owners of a LLC have the liability protection of a corporation. A LLC exists as a separate entity much like a corporation.

Owners are called members and not partners or shareholders. They are protected from some or all liability for acts and debts of the LLC *(this is dependant upon your state shield laws).* They cannot be held personally liable unless they have signed a personal guarantee.

The number of members are unlimited and may be individuals, corporations, or other LLC's.

The federal government does not recognize a LLC as a classification for federal tax purposes. A LLC business entity must file as a sole proprietor, partnership, S corporation or C Corporation providing a great deal of flexibility with taxation.

A LLC has pass- through taxation ***(no double taxation)***, unless the LLC elects to be taxed as a C Corporation. Using default tax classification, profits are taxed personally at the member level, not at the LLC level. All of your business losses, profits, and expenses flow through the company to the individual members. You avoid the double taxation of paying corporate tax and individual tax.

If you plan to set up a limited liability company, you will have to file articles of organization with the Secretary of State and pay the required fees.

Although it is not required in many states to draft an operating agreement, it is advisable. The operating agreement can help define your company profit sharing, ownership, responsibilities and ownership changes.

Corporations:

> Definition: a legal entity that is created under the laws of a State designed to establish the entity as a separate legal entity having its own privileges and liabilities distinct from those of its members.

A Corporation is <u>**limited liability**</u>. This further allows Corporations to raise large amounts of finance for their enterprises by combining funds from many owners of stock. It also reduces the amount that a shareholder can lose in a company. Their losses cannot exceed the amount that they contributed to the Corporation as dues or payments for shares.

Corporations exist as fictitious persons, granting a limited protection to the actual people involved in the business or corporation. If a corporation fails, shareholders normally only stand to lose their investment and employees will lose their jobs, but neither will be further liable for debts that remain owing to the corporation's creditors.

A corporation may issue stock, either private or public, or may be classified as a non-stock corporation. If stock is issued, its shareholders will usually govern the corporation, either directly or indirectly. The most common model is a board of directors that makes all the major decisions for the corporation.

There are three major types of Corporations: ***Close, C and S.***

1. **Close Corporations:** These corporations issue stock, but the amount of shareholders is greatly limited, usually to less than thirty. Given the small number of shareholders, normally all are involved in board-level decision making. Transfer and sale of stock is also tightly controlled.

2. **C Corporations:** These corporations theoretically allow for unlimited amounts of stock to be issued and usually have a smaller board of directors that make decisions. They pay taxes both at the corporate level and the personal level as the shareholders pay taxes on their dividends.

3. **S Corporations:** These corporations are identical to C Corporations but they have a special tax status with the IRS. Instead of paying taxes at both levels they are required to only tax their dividends *(the corporation itself does not need to pay taxes)*

The assets and structure of a Corporation may continue beyond the lifetimes of its shareholders and bondholders.

Comparison table

Limited Liabilities and Corporations

Limited Liabilities	*Corporations*
Much less administrative paperwork and record keeping than a Corporation	Corporations are required to keep formal minutes, have meetings and record

	resolutions.
LLC's have members.	Corporations are run by a group of stockholders
A LLC is dissolved when a member dies or undergoes bankruptcy,	Corporations can live forever. This allows stability and the accumulation of capital.
The number of members are unlimited and may be individuals, corporations, or other LLC's.	Depending on the type of Corporation the amount of shareholders can be limited.
Check the box taxation: LLC can be filed as a sole proprietor, partnership, S Corporation or C Corporation. (provides more flexibility)	Corporations are taxed as either Close, C or S Corporations.
LLC's do not have stock options.	Corporations have stock options.
LLC's has pass- through taxation.	Corporations can experience double taxation.
LLC's members are protected from some or all liability for acts and debts of the LLC *(this is dependant upon your state shield laws).* They cannot be held personally liable unless they have signed a personal guarantee.	If a corporation fails, shareholders normally only stand to lose their investment and employees will lose their jobs, but neither will be further liable for debts that remain owing to the corporation's creditors.
Although it is not required in many states to draft an operating agreement, it is advisable. The operating agreement can help define your company profit sharing, ownership, responsibilities and ownership changes.	The most common model is a board of directors that makes all the major decisions for the corporation.