

## Legal Business Structures

**Sole Proprietorship:** The very simplest business structure. Business is wholly owned by one person, the business and the sole proprietor are one and the same. The individual represents the company legally and fully. The business' assets are the personal possessions of the sole proprietor, the business' risks are the proprietor's risks, and the business' taxes are recorded simply as an addendum (Schedule C) to the proprietor's personal tax return.

**The Corporation:** When forming a corporation, you need to decide which corporate type to form. The two basic types of corporation are the S Corporation (S Corp) and the C Corporation (C Corp). In most aspects they are identical. The C Corporation is the basic type of corporation. The tax treatment is the primary difference between C Corporation and the S Corporation.

C Corporations are the most common type of corporation in the United States. They allow for theoretically unlimited amounts of stock to be issued, and usually have a smaller board of directors which make decisions. C corporations pay taxes both at the corporate level, and at the personal level, as shareholders pay taxes on their dividends.

S Corporations are C Corporation that received S Corporation status after filing form 2553 with the IRS. Instead of paying taxes at both levels, S Corporations are required only to tax their dividends--the corporation itself does not need to pay taxes. So the S Corporations is taxed in a pass-through manner, like members in a partnership, rather than as a regular corporation taxed on its own basis. The shareholders report the S Corporation's profit or loss on their individual tax returns. Some states may require an additional filing form for "S Corporation Status" along with the federal 2553 form.

**Limited Liability Company (LLC):** A LLC is a legal form of business that provides limited liability to its owners. It could be an individual, a partnership or a corporation. Often incorrectly called a "limited liability corporation" (instead of company), an LLC has certain characteristics of both a corporation and a partnership. The primary characteristic an LLC shares with a corporation is its limited liability, and the primary characteristic it shares with a partnership is the treatment of pass-through taxation. It is often more flexible than a corporation, with a less rigid structure of operating.

**Partnership:** There are several different types of Partnerships. There is a Limited Partnership, a Limited Liability Partnership, and a General Partnership.

Limited partnerships are partnerships in which it must have one or more general partners who manage and contribute to the establishment and the ongoing operation of the business and who are personally liable for partnership debts. A limited partner is one who invest, does not participate in the daily operation of the business, and is liable only up to the amount of his/her investment. The limited partner generally has limited or no managerial authority when it comes to the daily operation of the business. The limited partnership is considered one of the most common types of business structures.

It is not unusual for people to confuse a limited partnership with a limited liability partnership. The main difference is that with a limited liability partnership, all partners have some type of limit on the extent of their liability. With a limited partnership, at least one partner is classified a general partner and thus assumes more liability than any of the limited partners.

The most basic form of a partnership is a General Partnership, in which all partners manage the business and are personally liable for its debts; they share in both the profits and the losses. The legal definition of a partnership is generally stated as "an association of two or more persons to

carry on as co-owners a business for profit" (Revised Uniform Partnership Act § 101 [1994]) A General Partnership does not have limited partners. For a General Partnership, there is no registration with the state or even written agreement necessary for a general partnership to be formed, partnerships can be formal, where each party's roles and obligations are spelled out in a written agreement, or informal, where the roles and obligations are assumed or agreed to verbally. It is recommended, if you are forming a partnership you should always have a partnership agreement. Most of the law of General Partnerships applies to Limited Partnerships. With regard to taxes, the partnership is not a separate taxable entity, but instead the profits pass through to the partners who pay for them as income tax.