



# Entity Structure Guide



## What's The Best Entity Choice For Your Business?

A principal consideration for any new or existing business is choosing an appropriate legal entity. Available options in most states include C corporations, S corporations, general and limited partnerships, limited liability companies (LLCs), limited liability partnerships (LLPs) and sole proprietorships.

### Tax Implications

Each entity type has advantages and disadvantages. It's important to consider the tax implications. A certain type of entity can minimize your taxes. Understanding the total tax situation, including income tax, payroll tax, and estate tax exposure, is essential when determining the choice of entity.

Personal liability protection is often an owner's main objective in choosing the appropriate entity. Operating as a proprietorship or general partnership offers no owner liability limitation. Limited partnerships, LLCs, LLPs, S corporations, and C corporations provide varying degrees of liability protection for the owners, depending on state law. For sole owners, the single-member LLC is a popular liability-limiting alternative to a proprietorship.

If a business is owned by more than one individual, it cannot be run as a proprietorship. If all owners provide management services, a limited partnership is not a viable option, because that would jeopardize their status as limited partners. Limited partnerships, LLPs, LLCs, C corporations, and S corporations allow for management by multiple individuals without limitations.

### Get Ready For Succession

In many cases, an entity status change is sought to accomplish a transition in ownership. Whether the objective involves moving ownership to a successor via gifts, an installment sale, a stock redemption, a bequest, or a combination of methods, it is often necessary to use a different form of entity to meet these objectives. Each entity selection situation is unique. The business owner's objectives must be systematically matched with the various entities' attributes. All major tax and nontax issues must be considered and alternatives explored before choosing the appropriate structure for your business.

As with most business decisions, planning can have a positive, lasting effect on your venture. Contact us with questions about the appropriate entity structure for your existing business, a business you intend to purchase, or a contemplated new start-up business.

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	Sole Proprietorships and Single Member LLC	Partnerships	Limited Liability Companies (LLCs) and Limited Liability Partnerships (LLPs)	S Corporations (greater than 2% shareholder)	C Corporations
<b>Income Taxation</b>	Income is included on the owner's individual tax return.	Income flows through to each partner's individual tax return.	Income flows through to each member's tax return unless the LLC elects to be taxed as a corporation.	Income flows through to each shareholder's individual tax return. In some instances, taxation can occur at the entity level.	C Corporations are taxed on their earnings and shareholders are taxed on any dividends they receive.
<b>Liability</b>	A sole proprietor generally is not protected from liability.	General partners are subject to unlimited liability. Limited partners have liability only to the extent of their investment or contract law.	Members' personal liability is limited to the amount of their investment. State law supersedes.	Shareholders' personal liability is limited to the amount of their investment.	Shareholders' personal liability is limited to the amount of their investment.
<b>Self-Employment Tax</b>	The owner's net income is fully subject to self-employment tax.	General partners are subject to the tax on partnership income, but limited partners usually are not.	Members are generally subject to the tax except those qualifying as limited partners had the entity been a limited partnership.	Shareholders with income from their proportionate share of company earnings are not subject to the tax; salaries are subject to payroll taxes.	Does not apply.
<b>Deductibility of Losses</b>	If the owner materially participates, losses are deductible up to basis and risk limitations. The owner may carry back or forward net operating losses.	Generally, materially active partners can deduct losses, up to their basis, at risk, and passive limitations.	If an LLC is taxed as a partnership, the loss rules follow partnership rules.	Shareholders can deduct losses to the extent of their basis. Passive and at-risk limitations apply.	As a separate taxpayer, corporations can deduct losses or carry them back or forward to offset income in profitable years.
<b>Special Considerations</b>	Because business income or loss flows through to the owner's personal tax return, other items (such as deduction limitations) can be affected.	Income from a partnership is taxable regardless of whether partners receive an equivalent amount of cash as a distribution.	Generally, LLCs have the flexibility of partnerships with the limited liability of corporations.	The maximum income tax rate is the same as that for C Corporations (35% once the lower graduated brackets are phased out). Maximum of 100 shareholders.	Income can be subject to an alternative minimum tax of 20%.
<b>Accident and Health Insurance</b>	Generally, 100% deductible on 1040.	(1)	(1)	(2)	
<b>Dental Insurance</b>	Generally, 100% deductible on 1040.	(1)	(1)	(2)	
<b>Long-Term Care Insurance</b>	Generally, 100% deductible on 1040. Subject to limitations based on age of insured.	(1)	(1)	(2)	

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<b>Cafeteria Plans (\$125 Plan)</b>	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	
<b>Medical Reimbursement Plan</b>	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	
<b>Group Term-Life Insurance</b>	Only employees are eligible; owner is not considered an employee.	(1) (3)	(1) (3)	(2) (3)	(3)
<b>Disability Insurance</b>	Only employees are eligible; owner is not considered an employee.	(4)	(4)	(4)	(4)
<b>Deferred Compensation</b>	No	No	No		
<b>Retirement Planning</b>	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.	Only employees are eligible; owner is not considered an employee.		
<b>Qualified Retirement Plans</b>	An independent contractor can participate in his or her own plan, but cannot participate in another company's plan as an independent contractor of that company				
<b>Generally deductible by entity. Benefit would not be taxable to owner.</b> (1) If the payment is for partner (member) performing services for the entity, then the expense is a guaranteed payment deductible by the entity and taxable to the partner (member). If not, the payments are deemed distributions. Guaranteed payments are subject to self-employment tax. (2) The cost must be added to the owner's gross wages and is deductible by the S-Corp. The cost is subject to income tax (for the owner) and payroll taxes (the cost of accident and health insurance and long-term care insurance is not subject to payroll taxes). (3) Only the first \$50,000 of coverage is tax-free for employees. (4) If disability insurance is paid personally by the owner, any benefits would be tax free. If the entity pays for the insurance, any benefit would be taxable.			<b>Disclaimer</b> This guide (prepared only on a federal basis) provides summary information and is based upon information available at the time of preparation. The tax code and other laws may change or be subject to alternative interpretation at any time. The information is provided without any warranties, express or implied, and is therefore not warranted to be accurate, timely or complete. Check with your legal and tax advisors before implementing any action based upon the information provided. Any tax advice contained in the body of this document was not intended or written to be used, and cannot be used, by the recipient for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code or applicable state or local tax law provisions. <i>The information contained herein is confidential and proprietary to SVA Certified Public Accountants, SC. It is not to be disclosed, in whole or in part, without the expressed written consent of SVA Certified Public Accountants, SC. It shall not be duplicated or used, in whole or in part, for any purpose other than to evaluate the suggestions of SVA Certified Public Accountants, SC. Prepared 1/5/2016.</i>		