

Asset Protection - S Corps & LLCs

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S CORPORATION

S corporations are separate legal entities formed under state law in the same manner as C corporations. With the primary exception of taxation, S corporations are generally treated in the same way as C corporations with regard to liability protection and other corporate law matters. The tax ramifications of S corporation status are, however, very important. For the most part, with the exception of certain state issues and a few specific instances, the S corporation does not pay its own income tax. Instead, the tax nature and amounts of the business transactions are divided up according to the ownership of the corporation. The resulting income tax is paid by the shareholders directly on their individual tax returns. This can be a very significant advantage in that it avoids the “double taxation” problem for C corporations, while still providing the owners with liability protection.

The company's treatment as an S corporation is achieved by having all of the owners, including spouses, sign and file their election on federal form 2553 on or before the 15th day of the third month of the tax year in which the election is to take effect. If S corporation status is desired for a new entity, this formal election should be made as part of the incorporation process so as to not miss the filing deadline. S corporations can not have partnerships, other corporations or foreign residents as shareholders. They are also limited to no more than 75 shareholders. The S corporation is generally an excellent choice of entity for most small businesses.

LIMITED LIABILITY COMPANY

The Limited Liability Company (LLC) is a relatively new form of business ownership. In general terms, it provides partnership tax treatment and the avoidance of “double taxation” while protecting all of its members from liability for business obligations. In addition, the LLC does not have the ownership or structural limitations required for S corporation status. The lack of prior history, regulations and court cases for the LLC makes the legal and tax issues somewhat less secure than with the other entity structures.

As with corporations, the state of formation can be very important for the LLC. State laws have significant differences that may have an important effect on your entity selection. Legal counsel familiar with these matters and your particular business and business plan should be consulted prior to formation of the LLC. The LLC is an excellent vehicle for ownership of real property.