

WHAT IS THE DIFFERENCE BETWEEN S CORP AND LLC?

When you start a business, one of the first things you need to do is decide on a form for your business. Do you register as a sole proprietor, an LLC or a corporation? If you decide to become a corporation, do you go with a regular corporation, or an S corporation?

Most people understand what a sole proprietor and a corporation are, but are unsure about the LLC and S corporation. They look very similar, but vary in different aspects. It is important to be aware of these differences when you are making the decision about the structure of your business, or you could run into trouble down the road, and face trouble trying to change your business to the structure that works well for your business.

- **SIMILARITIES**

The first way in which they are similar is that both forms have pass through taxation. This means that the business is not taxed on their own income. Earnings are taxes on the individual's return and taxes are paid at the individual tax rate. Therefore, while you may have to file a tax form for these types of organizations, you end up paying taxes at individual rates.

Secondly, both organization types have state requirements of annual reports and fees. You do have to register your business with your state, and possibly with your city or county. In addition, both forms do provide some shield on your personal assets, which means you are not usually personally liable for business debts and liabilities. A word of caution: it never hurts to have some professional liability insurance to provide a shield against a lawsuit that may come about because of your business operations.

- **DIFFERENCES**

However, there are more differences than similarities between an S corporation and an LLC. For instance, there are more regulations about operations for S Corp. There are state rules about how to issue stock, as well as regulations for holding annual director and shareholder meetings with the minutes being kept as part of the corporate records. For an LLC, this is not required, but it is recommended that they have an operating agreement if more than one owner.

Speaking of owners, there are no limits to the number of owners that can be a part of an LLC, but S corporations are restricted to 100 shareholders. In addition, S corporation shareholders must be US citizens, whereas there is no such restriction for an LLC. Furthermore, an LLC can have subsidiaries, whereas S corps are barred from doing so. Ownership in an S Corp is easily transferrable by a sale of stock to a

qualified person. An LLC ownership is very hard to transfer, and usually requires the approval of any other owners.

There are also differences in how the owners can run the business. An LLC can have the owners manage the business, or delegate the management of the company to managers. An S corporation will have directors that make up a board of directors that oversees the officers they appoint to run the company. The key question to ask is how you want your business run, by the owners or some professional managers.

When you organize your business, you need to think about succession planning. Do you want to pass ownership on to someone, or let the business die when you do, or at least when you retire? S corporations can have a perpetual life, with ownership passing to whomever owns the shares, but LLCs usually end when the owner or owners die or withdraw from the organization. If you want to pass the business on to your kids, an S corporation will have stock that can be easily passed on to your children, giving them a share in the ownership of the business.

Lastly, with regard to taxes, with an S corporation, an owner can be treated an employee and be paid a salary, with any applicable taxes being withheld from their salary. Any corporate earnings after salary might be considered unearned income not subject to self-employment taxes. For an LLC, all earnings are subject to self-employment taxes, which may add some dollars to your tax bill. You will have to determine

what makes more sense for your particular situation, self-employment taxes on the business income, or a salary with taxes being withheld from a paycheck.

Deciding your company's structure is not something to be taken lightly. We advise that you think through the options, and are available to walk you through, and aid with, the setup of your business. We enjoy helping our clients build their businesses, and would love to help you with yours.

Need More Help Making This Decision?

Contact Us;

MY SMALL BUSINESS ACCOUNTANTS

6057B Arlington Blvd,

Falls Church VA, 22044.

705-534-6040, 202-293-4032