

# Business Ownership

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# Business Ownership

## □ OPTIONS

- *Sole Proprietorship (aka “disregarded” entity)*
- *General Partnership (GP)*
- *Limited Liability Company (LLC)*
- *Limited Partnership (LP)*
- *Limited Liability Partnership (LLP)*
- *Corporations*
  - C Corporation
  - S Corporation (No business entity starts out as an S corporation. Need to file for election with the IRS - Form 2553)
    - ✓ No more than 100 shareholders
    - ✓ None of the shareholders can be nonresident aliens
    - ✓ Only one (1) class of stock
    - ✓ None of the shareholders can be other corporations or partnerships

# Business Ownership

- Options (cont.)
  - Non-Profit Corporations
  - Professional Entities
  - B Corps

# Business Ownership

## □ *Decision Making Tree*

- *Ease/Cost to Form*
- *Personal Liability*
- *Business Income Tax*
- *Employee Expense Opportunities*

# Business Ownership

- ***Sole Proprietorship (“disregarded” entity)***
  - Unlimited personal liability
  - Pass through profit and losses
  - You earn what’s left over after all other expenses are paid (no W-2 option)
  - Self Employment Tax (beware)
  - **NEWS FLASH!!!** - Starting in 2018, owners may deduct up to 20% of net business income from personal income taxes. There are limitations which we will discuss later on in the workshop.

# Business Ownership

## □ *General Partnership*

- Relationship entity of 2 or more people
- Personal Liability
  - Partners personally liable - business debts and court judgements
  - Partners can be sued for full amount of any business debt or court judgement
  - Partners can bind the whole business to a contracts for business debt
- Taxes - Pass Through
  - K-1 form provided to partners, indicating their share of earnings
  - File information return - Form 106
- **Same NEWS FLASH!! As for Sole Proprietors**
- Expenses/Employees
  - Can have employees
  - Partners are not employees; thus, no W-2

# Business Ownership

## □ *General Partnership*

- You should (strong emphasis) have an agreement, including
  - Partners roles in signing and authorizations
  - Duties and responsibilities of each partner
  - Contributions of capital - time, money and assets
  - Rights to distributions, profits, compensation and losses
  - Unanimous vote requirements
  - Dissolution or exit strategy
  - Buy-sell agreement
  - Expulsion provision
  - Noncompete provision (not enforceable in California)
  - Miscellaneous provisions; i.e., who pays attorney's fees, mediation or binding arbitration clause.

# Business Ownership

## □ *Limited Liability Company*

- Created by state statute
  - Single member and multiple member LLC's
- Formation procedures
  - Reserve name
  - File articles of incorporation
  - Create operating agreement
  - Parties involved are called members
- Personal Liability
  - Members are not liable for business debts and court judgements
  - Members cannot be sued for full amount of any business debt

# Business Ownership

## □ *Limited Liability Company (cont.)*

- For Income Tax Purposes, can elect to be treated as,
  - “Disregarded” entity; like sole proprietorship (single member LLC)
  - General partnership
  - S Corporation
  - Form 8832 needs to be filed with IRS if single member LLC wants to be treated as an entity separate from its owner; similar for 2 or more member LLC’s if they want to be treated as a corporation
  - Generally, pass through entities
  - Major benefit to owners if elect to be treated as an S corporation
    - ✓ Shareholders - whose dividend is not subject to employment taxes
    - ✓ Also employees with pay and benefits commensurate with their position.
- **Same NEWS FLASH!! for 2018 - Tax Cuts and Jobs Act**
  - Not available to professional service companies
  - There are limits based on combined taxable income
- For all LLC and all subsequent partnership-type structures remember the \$800 minimum tax!

# Business Ownership

## □ *Limited Liability Company (cont.)*

### ○ Expenses/Employees

- Can have employees
- Members must perform direct and consistent management services to receive additional status of employee.
- However, if they elect to be treated as a S corporation, owner(s) can be both business owners (earning money as a shareholder) and employee. An employee must be compensated with a reasonable salary and is entitled to all of the benefits the company offers other employees.

# Business Ownership

## □ *Limited Partnership*

- Must have at least one (1) General Partner and one (1) Limited Partner
  - General Partner control day-to-day operations
  - General Partners are personally responsible for business debt and court judgements
  - Limited Partners
    - ✓ Do not play an active role in the business
    - ✓ Are not personally liable
    - ✓ Pay taxes on their share of earnings
    - ✓ Warning - Can become personally liable if they do not stick to their passive role
    - ✓ There are “carve out” provisions in some states allowing Limited Partners to vote on matters like removal of General Partners, terminating partnership, sale of assets without jeopardizing Limited Partner status.

# Business Ownership

## □ *Limited Liability Partnership*

- All owners are provided with limited liability
- Professionals, like lawyers and accountants prefer this alternative because they don't want to be personally liable for another partner's problems, particularly those involving malpractice claims
- Form at the state level - required to file a certificate of limited liability partnership in California
- Income taxes same as Limited Partnership

# Business Ownership

## ☐ C Corporation

- Formation Procedures
  - Create and File Articles of Incorporation
  - File IRS Form SS-4 to Obtain EIN (same form used for other entities)
  - Set up Corporate Records Book
  - Hold First meeting of Board of Directors
- Shareholders have limited personal liability
- Corporate Income Taxed Twice
  - Corporate
  - Personal
- **NEWS FLASH!! Does not apply**

# Business Ownership

## □ *S Corporation*

- Not a business formation structure; must elect to be treated as an S corporation by the IRS
- See notes in introductory slide
- Owner can be both,
  - Shareholder (and earn dividends)
  - Employee (and be paid a salary and provided with benefits)

# Business Ownership

## □ Other

- Professional Corporation
  - Owners have no personal liability for malpractice of other owners
  - All owners must belong to the same profession
- Non-profit Corporation
  - May not have to pay income tax (depends on purpose of organization)
  - Allowed purposes (for no income tax option)
    - ✓ Charitable
    - ✓ Scientific
    - ✓ Education
    - ✓ Literary
    - ✓ Religious
    - ✓ Other - testing for public safety; fostering sports competition; preventing cruelty to children or animals
  - Property transferred to corporation stays there. If corporation ends, property must go to another non-profit