

## **An Introduction to Business Organizations**

The United States Small Business Administration estimates that 627,000 new businesses were formed in the U.S. in 2008. Are you thinking about forming your own business? If so, this guide book can help understand the basic forms that a business can take.

At Behrend and Ernsberger, P.C., we have the necessary experience and skill to help you avoid the potential traps of incorporation. We will help you from start to finish: we will help you select the form of your business, draft the incorporating or registration documents, draft the bylaws or operating agreement, explain the tax structure, and discuss ways that you may potentially be liable.

The following is a discussion of some of the different forms that a business may take.

### **Corporation**

The corporation is a very powerful business organization structure. It is almost a living, breathing thing. It can be founded by one person or by thousands. In fact, it is so powerful that it is considered a "person" in many aspects of the law, including for First Amendment free speech purposes. A corporation is created by filing the appropriate registration papers and bylaws with the state. The management structure of a corporation involves directors, managers, and shareholders. Directors sit on the board of directors of a corporation. Managers are commonly the President, Vice President, Secretary, and Treasurer. Shareholders are the owners of the corporation and own stock. If you are starting a business by yourself, you can be chairperson of the board of directors, president, and the sole shareholder. Shareholders are the investors of the company, and a corporation raises capital by issuing and selling stock. In return for their initial investment, in the future, the corporation may decide to pay dividends to the shareholders. Directors and managers owe the fiduciary duties of care and loyalty to the corporation.

The hallmark of the corporation is that liability is limited to the assets of the corporation. This means that everyone involved in the management of the company is insulated from liability for business decisions, while shareholders only lose the value of the money they paid in. In some circumstances, corporations that refuse to obey the corporate form can expose officers, directors, and shareholders to liability.

The corporation has its own tax structure and a separate filing, so any money that you take from the corporation as a salary must be declared on your personal income tax return. Dividends are taxed at the individual and corporate level. There are many advantages and some disadvantages to incorporating. The legal team at Behrend and Ernsberger, P.C. will help you decide if the corporation is the best structure for your business.

### **S-Corporation**

Corporations with a small number of shareholders may be able to elect to be declared "S-Corporations." An S-corp is a corporation eligible to elect to be taxed at the shareholder level.

In essence, it is basically taxed like a partnership, so profits and losses are only taxed at the individual level. The corporation itself is not taxed at all.

The advantage of creating an S-corp is that the S-corp preserves the concept of limited liability for the individuals in charge of the corporation for business decisions. However, there are restrictions on the types of corporations that may elect to S-corp status. To name just a few, there must be fewer than 100 shareholders, all shareholders must be "allowable" (no corporate shareholders), and there may be only one class of stock. The legal team at Behrend and Ernsberger, P.C. can help you determine if your business could qualify as an S-corp.

### **Limited Liability Corporation**

The Limited Liability Corporation (LLC) is a particularly flexible organizational structure that allows for "check the box" taxation, meaning that the LLC may choose to be taxed as an individual, corporation, or partnership. The LLC allows the corporate owners, known as "members" or "managers," to limit their liability to the extent of their investment. It also enables the LLC to avoid double taxation. If the LLC so elects, tax on profits will only be assessed to the member on his or her personal tax return. Professionals commonly form LLCs. The LLC can also be converted to a corporation. The legal team at Behrend and Ernsberger, P.C. will help you decide if the LLC is the best structure for your business.

### **Partnership**

The partnership is another powerful business organization structure. A partnership must have at least two partners, but there is no maximum limit on the number of people who may be partners. A partnership is formed by filing the appropriate registration papers with the state and the creation of an Operating Agreement (O/A). Partners are jointly liable for the responsibilities of the partnership as set out in the O/A. It is possible for one partner to be solely an investor and one partner to be solely the operator of a partnership. Partnerships feature pass-through taxation, meaning that partners report their income from the partnership on their personal income tax returns. One of the key advantages of forming a partnership is the flexibility in the organizational structure. The legal team at Behrend and Ernsberger, P.C. will help you decide if a partnership is the best structure for your business.

### **Limited Liability Partnership**

The Limited Liability Partnership (LLP) is a specialized form of partnership, in which there must be at least two people, at least one of whom must designate a general partner. There is no limit on the number of general or limited partners, so long as there is at least one general partner. The advantage to forming an LLP is to the limited partner. Generally, the limited partner is only an investor in the business, and the LLP structure allows the limited partner to limit liability to the amount of the investment. However, the general partner is still fully liable. The LLP structure makes your business more attractive to investors and may help you raise capital. The legal team at Behrend and Ernsberger, P.C. will help you decide if the LLP is the best structure for your business.

## **Non-Profit Corporation**

The term "501(c)(3)" refers to a specific provision in the Internal Revenue Code. It allows for corporations to avoid tax liability as long as none of its earnings are distributed to private shareholders or other individuals. Of course, officers and employees are allowed to be paid a salary. However, the purpose of the organization cannot be for private benefit. Attaining 501(c)(3) status can be a lengthy procedure and involves complex filings. The legal team at Behrend and Ernsberger, P.C. will help you determine if your company could be eligible for a 501(c)(3) designation.

## **Sole Proprietorship**

It is possible to simply own your business without any complex organizational structure. The biggest advantage is that you don't have to ask anyone for permission to do anything, because it is your business and you aren't duty-bound to anyone else or to the organization itself. However, one drawback is that you may be completely liable for the debts, torts, and contracts of the business. The legal team at Behrend and Ernsberger, P.C. will help you decide if "going solo" is the best structure for your business.

## **Conclusion**

As you can see, there are many options for starting a business. Selecting the correct choice can feel like a daunting task, because there are risks and rewards with every selection that you make. To make the best possible choice, call the law firm of Behrend and Ernsberger, P.C. today at (412) 391-2515 for the sound legal advice that you need.