

Limited Liability Companies

There is a creative way of doing business that combines the advantages of a partnership and the liability protection of a corporation. It's called a limited liability company (or LLC).

A business can be conducted in a number of forms, such as a proprietorship, partnership, a regular corporation, or an S corporation. Doing business as a partnership has many tax advantages. Income is taxed only once, and there is great flexibility in how income and deductions are passed through to the partners. But the partners' assets are put at risk, since each general partner is personally liable for the partnership debts and obligations.

Corporations don't have the liability problem, since shareholders aren't responsible for debts of the corporation. However, a corporation's income may be taxed twice, once when the corporation earns it and once when it is distributed to the shareholders in the form of dividends.

Corporations are also required to maintain corporate records including the issuance of shares, board of director meetings as well as shareholder minutes. Limited liability companies are governed by a document called an Operating Agreement; therefore, less paperwork is required for an LLC.

Electing to be an S corporation oftentimes avoids double taxation. But S corporations have many restrictions on structure and possible disqualification as well as the need to maintain corporate records. The limited liability company, which is recognized by almost every state, offers a way out of this dilemma. Investors, known as members, own an LLC. It is managed either by the members themselves or by designated managers, usually entitled Managing Members.

Like shareholders of a corporation, the members' liability is limited to the amount of their investment. Yet, if the LLC is structured properly, it will be treated as a partnership for tax purposes. And there are no restrictions on the number and type of members, as there are with the shareholders of an S corporation.

If you are already doing business as one of the other entities, it may make sense to consider converting to an LLC.

*The purpose of this document is to provide general information, not legal advice. A qualified attorney should be consulted before implementing any plan.