Mariner
WEALTH ADVISORS

Choosing the Right Legal Structure for Your Business

What to Consider Before Launching Your New Company

Perhaps you're an entrepreneur with an exciting idea for a new business. Or maybe you and a family member or friend have been thinking about combining your varied talents and starting a business together. Either way, one of the first steps you will likely take is deciding which type of business structure will best meet your needs. The business structure you choose will impact almost every aspect of your business, including the paperwork you need to file, your daily operations, your taxes, your personal financial risk and your ability to raise money.

Do Your Research First

Of course, before you make this important decision, it's important to analyze your company's goals and research local, state and federal laws. Keep in mind that although you have the option of converting to a different structure in the future, it can be a cumbersome process that can have tax and other implications.

Here are a few of the most common business structures and pros and cons to consider:

Sole Proprietorship

A sole proprietorship is a simple business structure to set up. Although you don't have to take any formal action to form one, like all businesses, you do need to obtain any necessary licenses and permits.

As a sole proprietor, you are in control of your business and responsible for all your company's profits and debts. Because a sole proprietorship is not a separate business entity, the assets and liabilities of the company are not separate from your personal assets and liabilities.

Pros:

- Simple to set up
- Low cost
- Potential tax deductions
- Easy to exit

Cons:

- Personal liability for business debts and obligations
- Difficult to raise capital

Partnership

A partnership is a single business in which two or more people own a company together. There are two common types of partnerships:

- **Limited partnership (LP).** This business structure allows for one general partner with unlimited liability; all other partners have limited liability from debts against the partnership and the actions of other partners, but they also have limited control.
- **Limited liability partnership (LLP).** An LLP is structured similarly to an LP, but every partner has limited liability.

Because a partnership involves two or more individuals in the decision-making process, it's essential to develop a comprehensive partnership agreement. The partnership should define who owns what portion of the firm, how profits and losses are to be divided and should define how roles and duties are assigned. It's also a good idea to have your partnership agreement reviewed by a knowledgeable business attorney.

Pros:

- Easy to form
- Growth potential
- Special taxation

Cons:

- Loss of autonomy
- Limited control

Corporation

Legally, a corporation is a separate entity from its shareholder owners, which means it has its own legal rights. For example, a corporation can sue and be sued, own and sell property and sell its rights of ownership as stock. Additionally, the corporation, not the shareholders, is legally liable for the actions and debts of the business.

The different types of corporations include:

C Corporation

A C Corporation is owned by shareholders and as a separate entity, it can make a profit, be taxed and be held legally liable.

Pros:

- Strongest protection against personal liability
- Good choice for medium- to high-risk businesses and those needing to raise money

Cons:

- Higher cost to form than other entities
- Extensive recordkeeping, operational processes and reporting

S Corporation

Designed to help small businesses avoid the double-taxation of a C Corporation, the S Corporation is similar to a partnership or LLC. Under this business structure, profits (and some losses) can be passed through to owners' personal income without being subject to corporate taxes.

Pros:

- Limited liability protection
- Good option for businesses that would otherwise be a C Corp but meet criteria to file as S Corp

Cons:

- Need to file with IRS to get S Corp status
- Structure not recognized by some states

B Corporation

Also known as a benefit corporation, a B Corporation is structured to contribute to the public good and generate a profit for its shareholders. Although a B Corp's dual objective is different from a C Corp's sole focus on profit, the two entities are similar in how they're taxed.

Pros:

- Designed to make positive impact on society
- Structure recognized by majority of states

Cons:

- No tax advantage compared to C Corp
- Some states require B Corps to submit annual benefit reports

Closed Corporation

This type of corporation resembles a B Corp without the traditional corporate structure. A Closed Corporation is a privately held company typically run by a few shareholders.

Pros:

- More flexibility than a publicly traded company
- Limited liability protection

Cons:

- Shares usually barred by states from public trading

Nonprofit Corporation

As its name makes clear, nonprofit corporations do work that benefits society without focusing on earning profits. Some examples of nonprofits include charitable, educational, religious, literary and scientific organizations. In return for their emphasis on helping others, nonprofits—also referred to as 501(c)(3) corporations—can receive federal and state tax-exempt status.

Pros:

- Emphasis on benefiting society
- Not focused on making profits

Cons:

- Must file with IRS to get tax exemption status
- Needs to follow special rules about how to handle any profits

Limited Liability Company

A Limited Liability Company (LLC) combines the benefits of corporation and partnership business structures. It's an attractive option for business owners looking for the liability protection that corporations enjoy while allowing earnings and losses to pass through to their personal income, thereby avoiding corporate taxes.

Pros:

- Personal liability projection
- Profits and losses don't have to be divided equally among members
- Members pay lower tax rate than under a corporation structure

Cons:

- Members must pay self-employment taxes
- Some states may require LLC to be dissolved when members join or leave

Cooperative

Owned by the people it serves, a Cooperative, or Co-op, is operated for the benefit of its members, also referred to as user-owners. Members vote to decide on the Co-op's mission, and the profits and earnings are shared by its members.

Pros:

- Low taxes
- Eligibility for federal grants
- Discounts on products and services

Cons:

- Can be complex to form

Partner With Your Wealth Advisor

For assistance in setting up a business structure that aligns with your business goals, reach out to your wealth advisor. At Mariner Wealth Advisors, we offer a range of business advisory services to assist you, including business valuation, investment banking, tax reporting and financial reporting.

For more information visit: marinerwealthadvisors.com