

Table Comparing Different Legal Structures

This table compares the entity choices by looking at issues (tax and nontax) that generally are considered significant when selecting the type of entity to use for a new business.

| Issue | C Corp | S Corp | Partnership | LLC | Sole Proprietorship |
|---|--|--|---|---------------------------|--|
| Limited liability for owners? | Yes | Yes | No general partners, yes for limited partners. Limited partners cannot be actively involved in the business without losing limited liability. | Yes | No, liability is unlimited |
| Flexible ownership and capital structure? | Yes | No. Limited to 100 Shareholders and one class of stock. Types of shareholders limited. | Yes. Need at least two partners. | Yes. PA allows one member | N/A-one owner |
| Continuity of life for Entity? | Yes | Yes, but stock ownership must be monitored | Generally no | Often, yes | No |
| Centralized management of entity? | Yes | Yes, but number of stockholders limited to 75, so may not be practical. | No for general partnership, usually yes for limited partnership. | Often, yes | No |
| Free transferability of ownership interest? | Yes, but may be contractually limited by a buy/sell agreement. | Yes, but must observe limitations on who can own stock. | Generally, no. | Generally, no | No, but as practical matter, the entire business may be sold |
| Degree of administrative complexity? | High | High | Moderate | High, because of newness | Low |
| Certainty of legal and tax Outcomes? | High | High to moderate. | Moderate | Lowest, due to newness | High |
| Double Taxation of income? | Yes | No, unless former C corp. and built-in gains and certain other taxes apply. | No | No | No |
| Ability to retain income at lower current tax cost. | Yes | No | No | No | No |
| Tax treatment fringe benefits for owners? | Good | Poor, if own more than 2% of stock. | Poor | Poor | Poor |

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| Issue | C Corp | S Corp | Partnership | LLC | Sole Proprietorship |
|---|---|--|---|---|--|
| Potential ability to reduce payroll taxes of owner-employees? | No | Yes, within limits of reasonableness. | No | No | No, but may benefit from employing owner's children under the age of 18. |
| Potential favorable treatment of owner-level interest expense on debt to inject capital or acquire ownership interest? | No | Yes | Yes | Yes | Yes |
| Double taxation at state and local tax level? | Generally, Yes | Sometimes | Rarely | Sometimes | No |
| Additional owner-level tax basis from entity-level debt (for loss deduction purposes)? | No | No, even if owner guarantees debt. | Yes | Yes, but generally not for Section 465 at-risk purposes. | N/A, but owner gets basis from debt since no Entity exists. |
| Basis adjustments upon purchase of ownership interest? | No | No | Yes | Yes | N/A |
| High ability to make tax-free contributions and distributions? | No | No | Yes | Yes | Yes |
| Ability to make special tax allocations among owners? | No | No | Yes | Yes | N/A |
| Ability to shift entity income among family member owners? | No | To a degree, by manipulating wages of employee owners. | Yes, within limits of family partnership rules. | Yes, within limits of family partnership rules. | Yes, by employing family member. |
| Treatment of gain on sale of ownership interest? | Generally, capital unless collapsible corporation rules apply (IRA Sec. 341). | Capital | May be part ordinary under "hot assets" rules (See IRA Sec. 751). | May be part ordinary under "hot assets" rules (See IRA Sec. 751). | May be part ordinary due to recapture items. |
| Treatment of loss on sale of ownership interest? | Capital unless stock it Section1244 stock. | Capital unless stock it Section1244 stock. | Capital | Capital | Depends on nature of assets sold. |

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| Issue | C Corp | S Corp | Partnership | LLC | Sole Proprietorship |
|---------------------------------------|---------------|---------------|--------------------|------------|--|
| Flexibility to chose tax year? | Yes | Limited | Limited | Limited | Limited [See Jerome H Vance, TC Memo 1989-95, PH TCM 89095 (1989)] |

| | | | | | |
|--|---|--|--|--|--|
| Passive loss rules apply? | No, unless a PSC or closely held corp. | Yes, at shareholder level. | Yes, at partner level. Treatment of limited partners is unfavorable. | Yes, at member level; unclear if members treated as limited partners. | Yes |
| Deduction for corporate dividends received? | Yes | No | No | No | No |
| Loans against qualified plan accounts possible for owners? | Yes | No, if own more than 5% of stock. | No, if own more than 10% of profits or capital interests. | No, if own more than 10% of profits or capital interests. | No |
| Favorable tax rate on long-term capital gains? | No, regular corporate rates apply. | Yes, 28% maximum. | Yes, 28% maximum. | Yes, 28% maximum. | Yes, 28% maximum. |
| Double taxation upon liquidation? | Yes | No | No | No | No |
| Personal Holding company tax applies? | Yes | No | No | No | No |
| Accumulated earnings tax applies? | Yes | No | No | No | No |
| Unreasonable owner compensation issue applies? | Yes | Normally no, unreasonably low compensation could be challenged. | No | No | No |
| PSC rules apply? | Yes | N/A | N/A | N/A | N/A |
| Limitations on use of cash method? | Yes, but smaller corporations and PSCs can use cash method. | No, unless more than 35% of losses allocated to "limited entrepreneurs". | No, unless more than 35% of losses allocated to limited partners. | No, unless more than 35% of losses allocated to "limited entrepreneurs". | No |
| Limitations on use of NOLs and other "tax attributes" after ownership change? | Yes | N/A. Losses pass through to owners. | N/A. Losses pass through to owners. | N/A. Losses pass through to owners. | N/A |
| Entity-level ATM? | Yes | No, but ATM information must be provided to shareholders. | No, but ATM information must be provided to partners. | No, but ATM information must be provided to members. | No, but ATM information must be provided to calculation. |

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