

Choosing a Business Structure

Your dream business is mapped out in your mind. You might have even secured the money to order your first shipment of product or place your first ad in the newspaper. Everything seems to be falling into place, so you sit down to fill out your business license application. You are moving right along until you are asked to check the box that claims what type of business you have. Are you an Individual (Sole Proprietorship), Partnership, Limited Liability Company, or C-Corporation. What does all that mean? What should you check? Below is a quick guide to help you determine, or at least narrow down, what type of business structure is right for your company.

Sole Proprietorship - A business owned and operated by one individual. The individual reports the profits of the business on his/her personal income tax return.

Advantages:

- Relatively easy set-up. Usually only requires a local business license (unless you have employees)
- Very little government regulation
- All profits go to the owner

Disadvantages:

- The owner is personally liable for all debts of the business and could be held personally liable for a business-related lawsuit
- Once the owner passes away or loses interest the business ceases to exist
- The owner may fail to distinguish between personal finances and business finances making financial and tax preparation difficult

Partnership- A business made up of two or more people. The partners pay income tax on their share of the earnings.

Advantages

- Easy to set-up. Requires a local business license and registration with the Arizona Secretary of State.
- All profits flow through to the owners

Disadvantages

- Each owner is liable for 100% of the debts of the business
- Personalities between partners may become an issue. A written agreement should be made specifying each partner's initial investment, share of the earnings, and expectation.
- If one partner leaves the partnership is considered dissolved.

Limited Liability Company (LLC) – For tax and accounting purposes the LLC is treated like a partnership. For reasons listed below this method of structuring a business has become fairly popular.

Advantages:

- Personal assets of members of an LLC are protected from the creditors of the company.
- All profits flow through to the members

Disadvantages

- Must file Articles of Organization and an Annual Report with Arizona Corporation Commission

Corporation – A corporation is a legal business entity. To be an owner of a corporation you must purchase shares of stock. Common stockholders elect the Board of Directors and Board of Directors elects a president, vice-president, and a secretary-treasurer to conduct the business. (The shareholder can be on the Board of Directors and also elect herself to be the president).

Advantages:

- The corporation is responsible for paying taxes and obeying the law
- The corporation is continuous regardless of shareholders
- More prestigious
- Shareholder liability is only limited to the investment

Disadvantages:

- More expensive to create
- Highly regulated
- Taking money out of corporation is more complex. You can receive a dividend, but the earnings are taxed twice. You could loan out of the business, increase you salary, or get a bonus. All which must be approved by the Board of Directors.

Now go ahead and check that box!

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