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A PUBLICATION OF
FREEDOM FINANCIAL PARTNERS

AN INTRODUCTION TO

**Business
Entities**

THINGS TO CONSIDER WHEN SETTING UP YOUR NEW BUSINESS

Intro

About Freedom Financial Partners

Freedom Financial Partners understands the decisions and choices facing a new business. We have helped many businesses during the formation stage. Some questions you will need to consider:

- How will decisions be made? And by whom?
- What is the source for start-up equity funding?
- How will distribution of profits be handled?
- How and under what conditions can ownership be transferred?

There may or may not be a formal document to establish your business, but regardless these are the questions you should be asking yourself.

This book will describe the various business entity structure available, and provide some details regarding benefits as well as how and if a formal document is required. The document can be called many things: A Business Operating Agreement, the Bylaws, or a Partnership Agreement. The specific name and how formal the document may be is determined by the business entity you select.

Good luck with your business, and please contact us if we can help!

*Freedom
Financial
Partners*



CHAPTER ONE

**DEFINITIONS &
DESCRIPTIONS**

Definitions and Descriptions

Understanding the various business entities

If you want to start a new business you will need to think about what type of business structure you should choose.

The LLC

The term LLC is an abbreviation for Limited Liability Company, or Limited Liability Corporation. An LLC structure establishes a boundary between your personal assets and those of the business. This may prevent legal claims for business activities from impacting your personal finances and assets.

According to the IRS website, “A Limited Liability Company (LLC) is a business structure allowed by state statute. Each state may use different regulations, and you should check with your state if you are interested in starting a Limited Liability Company.

Owners of an LLC are called members. Most states do not restrict ownership, and so members may include individuals, corporations, other LLCs and foreign entities. There is no maximum number of members. Most states also permit “single-member” LLCs, those having only one owner.” The last sentence is affirming that many states allow you to be a sole proprietorship and an LLC.

NOTE: Each of the remaining business entity types discussed in this book may, or may not be, an LLC in addition to the business entity described. The IRS does not recognize an LLC as a business entity, it is necessary to **also** be a sole proprietorship, a partnership, a corporation or an S-Corporation.

The Sole Proprietorship

Many start up businesses are set up as sole proprietorships. This is the most basic business structure and offers many bookkeeping and tax advantages over more complex business entity types. As a sole proprietorship you are declaring that you alone are responsible for the financial responsibilities of your business. The owner personally applies for any loans or extension of credit required by the business.

The owner is responsible for all decision making and typically does not have a governing body, such as a Board of Directors, to report to or oversee business strategy or progress.

The Partnership

Partnerships are another business entity which requires minimal formal documentation. A partnership can be loosely formed by individuals wishing to go into business together. Governance may or may not be established in writing and the ownership percentages are not required to be equal among all owners.

Partnerships must request a Federal Employer Identification Number (EIN) which is used to establish bank accounts and financial records, including filing and paying income taxes. This is requested through the IRS, and can be accomplished using the online services functionality.

The Corporation

Forming a corporation requires the greatest level of documentation up front. Establishing governance and shareholder value are two key elements. Initial capital would be raised through the sale of stock to shareholders. A corporation must file with a State commission to come into existence. The application will include details regarding the structure, officers, governance, etc. The specifics of the application process will vary by state.

Corporations hire executives to run the company and answer to the shareholders. It is not uncommon for executives to also be shareholders, but this is not a requirement.

The S-Corporation

Forming an S-corporation is very similar to the corporation process.

The primary difference is the way financial results are tracked and taxes are paid. S-Corporations have officers, and it is a requirement of the S-Corporation business entity that officers receive a regular salary. The officers are also shareholders in the S-Corporation structure.

Table 1.1 – Summary of Business Entity Characteristics

Business Structure	Sole Proprietorship	Partnership	Corporation	S-Corp
Ownership	One Person	Multiple People	Shareholders	Shareholders
Documented Structure Required?	NO	NO	YES	YES
Responsible for Leadership	Owner	Partners	Hired Executive(s)	Officer(s)
Raising Initial Capital	Owner personally responsible	Partners personally responsible	Sale of stock	Sale of stock

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CHAPTER TWO

BENEFITS

Benefits

Understanding the business entities benefits

Each business entity offers benefits, and there is not a generic entity type to choose as a default.

The Sole Proprietorship

This may not be the business entity selection if the business has more than one owner. The owner having sole control and responsibility is a key benefit. In addition, sole proprietorships do not require a separate tax return for the business. The businesses income and taxes are incorporated into the owners personal return through the Schedule C.

The Partnership

Partnerships require less formal initial documentation than a Corporation or S-Corp entity. Another benefit is that the business earnings are taxed through the partners' personal returns. A Partnership return is filed and the partners income is reported on a K-1 form which is incorporated into the individual returns using Schedule E to report the K-1.

The Corporation

Corporations inherently provide the separation of business and owner financial responsibilities, making the need for an LLC moot. Corporations pay taxes directly on the businesses income. Executives receive W2 statements, and shareholders receive 1099-DIV for inclusion in their personal returns.

The S-Corporation

An S-Corporation does file a tax return, but the income is taxed through the owners returns using a combination of the K-1, similar to a partnership and the W2 for the salary paid to the officers/owners.

Table 2.1 – Summary of Tax Implication by Business Entity

Business Structure	Sole Proprietorship	Partnership	Corporation	S-Corp
Business Tax Filing	Schedule C of the owners return	1065 filed for the business	1122	1122-S
Business Profits are taxed	No additional requirement	NO	YES	NO
Owner(s) income is taxed	No additional requirement	Through use of the K-1	Executives receive W2s and shareholders receive 1099- DIVs	Officer(s) receive W2 & K-1s

Determining your business entity type is important, but you can change business structures by notifying the IRS without needing to close your business and restart as a new business.

STILL HAVE QUESTIONS?

As part of our ongoing commitment to the entrepreneur, Freedom Financial Partners will provide a free initial phone consultation.

In addition, we can help with actual start up documentation and state filing requirements.

Click below and we will be happy to set up a call. Or, go to our website www.freedomfinancialpartnersllc.com for additional free support.

CONTACT US!