



# FORMS OF BUSINESS ORGANIZATION

"Before you run in double harness, look well to the other horse" - Ovid



## Main Factors in Choosing a Form of Ownership

- Ease of transferring ownership
  - Sell/buy, gift, inherit
- Tax rates
  - Personal vs Corporate
- Liability exposure (risk)
  - Unlimited liability = your personal assets are at risk
  - Limited liability = you can only lose what you invested




## Major Forms of Ownership

- Sole Proprietorship
- Partnership
- Corporation
- Limited Liability Company



## "Hybrid" Forms of Ownership

- Limited Partnership
- S Corporation
- Cooperative

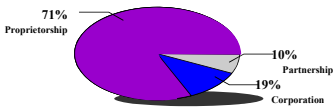


## Forms of Ownership

Most businesses are Sole Proprietorships

**Forms of Ownership (% of businesses)**

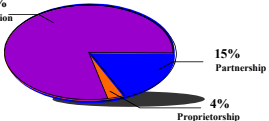
Source: Statistical Abstract of the United States, 2012, Table 744.



Corporations have higher levels of sales (\$)

**Forms of Ownership (% of sales)**

Source: Statistical Abstract of the United States, 2012, Table 744.



## Sole Proprietorship

A business owned/managed by one individual

<p><b>Advantages</b></p> <ul style="list-style-type: none"> <li>■ Simple to create</li> <li>■ Low start-up costs</li> <li>■ Taxed at personal rates</li> </ul>	<p><b>Disadvantages</b></p> <ul style="list-style-type: none"> <li>■ Unlimited liability</li> <li>■ Limited access to assets</li> <li>■ Hard to transfer ownership to another person</li> </ul>
--	---



## Sole Proprietorship

- Good form of organization for:
  - *Businesses with very little risk to others*
  - *Small, part-time, or temporary businesses*
  - *"Low budget" businesses*
- Hard to transfer to another owner
  - *Must sell the business to new owner or form a different type of organization (partnership, etc.)*



## Sole Proprietorship

- Examples:
  - *Most farms (85%) are sole proprietorships*
  - *Many roadside stands/markets*
  - *Other local businesses?*



## Partnerships

**2 or more people (or groups)  
who co-own a business**

### Advantages

- Relatively easy to establish
- Pooling of resources by owners
  - *Assets, Capital, etc.*
- Taxed at personal rate

### Disadvantages

- Unlimited liability
- Harder to transfer to others
- Potential for conflict among owners



## Types of Partners

### General Partners

- *Share in the ownership and management of the business*
- *Unlimited personal liability*
- *All partnerships must have at least one general partner*

### Limited Partners ("silent partners")

- *Investors who do NOT participate in the management*
- *Liability is limited to the amount they have invested*
- *Any number of limited partners are allowed*



## Partnerships

- Good form of organization for:
  - *Small/Medium-sized businesses*
  - *Temporary or short-term businesses*
  - *Businesses that do not face a lot of risk*
- Relatively easy to transfer ownership to the other partners
  - *Must form a new form of organization if you want to add new partners*



## Partnerships

- Partnerships can be:
  - *Informal*
    - No written partnership agreement between partners
    - NOT recommended!
  - *Formal*
    - Have a written partnership agreement about:
      - *Sharing profits*
      - *Ownership of the land, buildings, equipment, etc.*
      - *How to add/remove partners*



## Partnerships

- Examples of local partnerships:
  - General Partnership?
  - Limited Partnership?



## Corporations

**A separate entity, apart from its owners; may engage in business, make contracts, sue, be sued, and pay taxes**

### Advantages

- Limited liability of stockholders\*
- Unlimited lifetime
- Very easy to transfer

### Disadvantages

- Taxed at corporate rate
- May face double taxation (profits of firm and profits paid to owners are taxed)
- More legal requirements to establish

\* Your personal assets may still be at risk in lawsuits and/or foreclosure.



## Types of Corporations

- C Corporations
  - Corporate tax rates (usually higher than personal tax rates)
- S Corporations
  - Closely-held corporation (less than 75 shareholders)
  - Taxed at personal rates
- Cooperatives
  - Owner-members; one vote per owner-member
  - Profits are returned to owner-members



## Corporations

- Good form of organization for:
  - Large businesses
  - Businesses with several owners
  - Businesses that face a lot of risk
  - Businesses that want to stay in operation for a long time



## Corporations

- Examples of C Corporations
  - Ford, GM, John Deere, Home Depot,
- Examples of S Corporations
  - Many family farm corporations are S corporations
- Examples of Cooperatives
  - Farm Credit of the Virginias, Southern States, Best Western, Minute-Maid, many local utilities are co-ops



## Limited Liability Companies (LLC)

**Hybrid of a partnership and a corporation**

### Advantages

- Limited liability\*
- Taxed at personal rates
- No double taxation
  - Taxed at personal rates

### Disadvantages

- "Red-Tape" – can be confusing to create
- Relatively expensive to create

\* Your personal assets may still be at risk in lawsuits and/or foreclosure.



## Limited Liability Companies (LLCs)

- Good form of organization for:
  - Large businesses
  - Businesses with several owners
  - Businesses that face a lot of risk
  - Businesses that want to stay in operation for a long time
- Not much difference between LLCs, C-corps and S-corps



## So which is it gonna be?

- Main determinants:
  - Tax implications
  - Transferability of ownership
- You can make one form look almost identical to any other form
  - Get qualified legal & accounting assistance before choosing a form for your business

