

Lesson 2 - Introduction to Business Types

Bell Ringer: Name a situation when you would want to be in partnership with someone(s) in a business and name a time when you would not.

A. Section 1 – Review the Language of Business

1. Have the students define/apply the main terms.
2. Briefly review the things that businesses have in common (from the students' experiences)
 - need a market (customers)
 - need labor
 - requires money to get started....

B. Section 2 - Discuss types of business legal organization (Est. time 30-40 minutes)


1. Main factors in choosing a form of organization
 - a. Transferability of ownership to others
 - i. 3 main ways
 - a. Sell/buy a share of the business (assets, shares, etc.)
 - Very easy for corporations & LLCs – just sell your shares in the company
 - b. Gift a share of the ownership of assets to others
 - Very easy for corporations & LLCs – just gift your shares to others
 - Harder for sole proprietorships and partnerships
 - Must determine ownership of assets, keep good records
 - Hard to determine the value of these assets
 - c. Inherit a share of the ownership of assets from others
 - b. Taxation
 - i. 2 main types of income tax rates
 - a. Personal income tax rates
 - Usually lower than corporate tax rates
 - Sole proprietors, partnerships, most LLCs and S-corporations are taxed at personal rates
 - b. Corporate income tax rates
 - Mainly for C-corporations
 - ii. Double taxation can be an issue for C-corporations
 - a. Profits of the corporation are taxed at the corporate income tax rate
 - b. Dividends (profits returned to the owners/shareholders) are taxed at the personal income tax rates
 - c. This can be avoided or minimized with the help of an accountant. If you can pay the owners a higher salary instead of giving them a dividend, then you can reduce/eliminate the corporate profits (\$0 corporate income tax). The owners' salaries are taxed at the personal income tax rate

- c. Liability of owners in case of lawsuit or foreclosure/bankruptcy
 - i. This refers to how much of the owners' personal assets are at risk in the case of lawsuits or bankruptcy
 - ii. Unlimited Liability means that the owners are completely responsible for all damages and all debts of the business. The personal assets (house, autos, personal belongings, etc.) may be sold to repay the debts.
 - This is mainly an issue for sole proprietors and general partnerships
 - iii. Limited Liability means that the owner can only lose the amount of money that he/she has invested in the business. For example, if you own 10 shares of John Deere stock worth \$1,000, the maximum amount that you can lose in the case of lawsuit or bankruptcy is \$1,000. The courts and creditors cannot use your personal assets to repay the debts of the corporation.
 - NOTE: If the owners "co-sign" on the loans of the corporation, then their personal assets are now at risk. The owners of the corporation no longer have limited liability
- 2. Main types of organization (2-3 advantages and disadvantages of each type)
 - a. Sole proprietorship
 - b. Partnership (general/limited)
 - c. Corporation (S & C)
 - d. Limited liability corporation (LLC)
- 3. Have students try to give examples of each type

Materials: **PowerPoint presentation – for use as a handout if desired**
 Side-by-side chart for comparison
 In-class Exercise and Key
 Homework Exercise and Key
 A list of examples for each type of organization – developed by teacher
 Forms of Ownership Reading

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

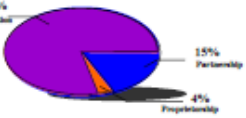
Most businesses are Sole Proprietorships

Forms of Ownership (% of businesses)
Source: Bureau of Economic Analysis, 2011, Table 1a.



Corporations have higher levels of sales (\$)


Forms of Ownership (% of sales)
Source: Bureau of Economic Analysis, 2011, Table 1a.



Sole Proprietorship

A business owned/managed by one individual

Advantages	Disadvantages
■ Simple to create	■ Unlimited liability
■ Low start-up costs	■ Limited access to assets
■ Taxed at personal rates	■ Hard to transfer ownership to another person



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**

<p><u>Advantages</u></p> <ul style="list-style-type: none"> Relatively easy to establish Pooling of resources by owners <ul style="list-style-type: none"> - Assets, Capital, etc. Taxed at personal rate 	<p><u>Disadvantages</u></p> <ul style="list-style-type: none"> ■ 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



Lesson 2- Types of Business Organizations
Notes Organizer

	Advantages	Disadvantages	Who is it good for?	Other
Sole Proprietorship				
Partnership -General Partners -Limited Partners				
Corporations				
C Corporation				

S Corporation	Cooperatives	Limited Liability Company (LLC)

Types of Business Organizations Worksheet

Directions: Utilize the presentation and notes to fill out the chart. You may also need to do some research of your own.

	Ease/Cost of Start-up	Ease of Transfer	Taxation	Liability
Sole Proprietor				
General Partnership				
Limited Partnership				
C- corporation				
S- corporation				
Cooperative				
Limited Liability Company (LLC)				

Types of Business Organization- Answer Key

	Ease/Cost of Start-Up	Ease of Transfer	Taxation	Liability
Sole Proprietor	Very easy Low cost	Difficult	Personal tax rates	Unlimited Liability
General Partnership	Easy Low cost	Difficult	Personal tax rates	Unlimited Liability
Limited Partnership	Moderate Low cost	Difficult	Personal tax rates	Limited liability for the limited partner. Unlimited liability for the general partners.
C-corporation	Harder Relatively high costs	Very easy	Corporate tax rates May face double taxation	Limited liability for owners
S-corporation	Harder Relatively high costs	Relatively easy	Personal tax rates	Limited liability for owners
Cooperative	Harder Relatively high costs	Moderately difficult	Corporate tax rates may apply	Limited liability for owners
Limited Liability Company (LLC)	Hardest Highest cost	Relatively easy	Personal tax rates (usually)	Limited liability for owners

Forms of Business Organization In-Class Exercise

Choose the most appropriate form of business organization for the following businesses. There may be more than one answer for each! Your choices are:

Sole Proprietorship (SP)

C-Corporation (C)

General Partnership (GP)

S-Corporation (S)

Limited Partnership (LP)

Limited Liability Company (LLC)

_____ Roadside produce market for a family farm operated only in the summer.

_____ Building construction company owned by several people who are not related.

_____ Medical Doctor/Office with 3 doctors

_____ A part-time woodworking business where you sell birdhouses, small furniture, yard ornaments, etc.

_____ A grocery store where 2 people want to own and manage the business, and 1 person wants to just invest \$50,000, but have no management responsibilities.

_____ A student who wants to sell flowers on the sidewalk outside of a local business.

_____ A transportation company that wants to limit ownership of the company to a few family members.

_____ A lawn-mowing business that is only operated for 1 summer.

_____ A landscaping business owned by 3 friends. The company installs very expensive landscapes in a wealthy neighborhood.

_____ A tree removal firm owned by 1 person. He cuts down trees next to houses, buildings, and power lines.

Forms of Business Organization In-Class Exercise (Key)

Choose the most appropriate form of business organization for the following businesses. There may be more than one answer for each! Your choices are:

Sole Proprietorship (SP)

C-Corporation (C)

General Partnership (GP)

S-Corporation (S)

Limited Partnership (LP)

Limited Liability Company (LLC)

- SP Roadside produce market for a family farm operated only in the summer.
- C, S, LLC Building construction company owned by several people who are not related.
- C, LLC Medical Doctor/Office with 3 doctors
- SP A part-time woodworking business where you sell birdhouses, small furniture, yard ornaments, etc.
- LP A grocery store where 2 people want to own and manage the business, and 1 person wants to just invest \$50,000, but have no management responsibilities.
- SP A student who wants to sell flowers on the sidewalk outside of a local business.
- S, LLC A transportation company that wants to limit ownership of the company to a few family members.
- SP A lawn-mowing business that is only operated for 1 summer.
- GP, C, S, LLC A landscaping business owned by 3 friends. The company installs very expensive landscapes in a wealthy neighborhood.
- C, LLC, SP A tree removal firm owned by 1 person. He cuts down trees next to houses, buildings, and power lines.

NOTE – there is usually not just one correct answer or one best form of organization for a business. C-corps, S-corps, and LLCs are very similar and can be formed so that they are almost identical.

Forms of Business Organization Homework Exercise

Please answer the following questions in a concise, meaningful manner.

1. What are the 3 main factors that you should consider when choosing a form of business organization for your operation?

2. Your entire class wants to start its own small business that does handiwork for low-income families in the community – mowing lawns, shoveling snow, painting fences, etc. The main goal of this business is to gain experience managing a real-world operation while helping improve the community. The work that you will be doing is very low risk – the chances of hurting someone or damaging property are very low. You will charge prices that are just enough to cover your expenses. Finally, you would like this business to continue for several years – long after you have graduated – you will pass the ownership of the business to younger students as you graduate.

What is the best form of business organization for your business? Please give 3 reasons why you selected this particular form of organization.

3. Find at least one example of a local business for each of the main forms of organization.

Type of Organization	Example of a Local Business
Sole Proprietorship:	_____
General Partnership:	_____
Limited Partnership:	_____
C-corporation:	_____
S-corporation:	_____
Limited Liability Company:	_____

4. Choose the owner of a local business – it can be someone from your family who owns a business. Briefly interview them about the form of organization of their business. Ask them questions such as:

What is the form of organization for your business?

What is the main reason you chose this form of organization?

What do you think is the biggest advantage of this form?

What do you think is the biggest disadvantage of this form?

Who did you talk to for advice before you selected this form of business organization?

Write a 1- to 2-page paper that summarizes your interview. Please include a brief description of the business. Also, include your thoughts into your paper: for example, do you agree with the choice of organization? What other type of organization might be appropriate for this business?; What did you learn from this interview....

Forms of Business Organization Homework Exercise (Partial Key)

Please answer the following questions in a concise, meaningful manner.

1. What are the 3 main factors that you should consider when choosing a form of business organization for your operation?

Ease of transfer of ownership to others

Taxation of the business' profits

Liability faced by the owners of the business

2. Your entire class wants to start its own small business that does handiwork for low-income families in the community – mowing lawns, shoveling snow, painting fences, etc. The main goal of this business is to gain experience managing a real-world operation while helping improve the community. The work that you will be doing is very low risk – the chances of hurting someone or damaging property are very low. You will charge prices that are just enough to cover your expenses. Finally, you would like this business to continue for several years – long after you have graduated – you will pass the ownership of the business to younger students as you graduate.

What is the best form of business organization for your business? Please give 3 reasons why you selected this particular form of organization.

Again, there isn't just one correct answer – great opportunity for a little “Debate”.

Main issues:

- not facing much risk
- will not be making a lot of profits (just covering expenses)
- want it to last for several years

To me, the main consideration is wanting it to last for several years – that would lead me to recommend a C-corp or S-corp (possibly an LLC) – this allows the graduating students to

pass their share of ownership to younger students. To me, liability and taxation are not primary factors.

- Find at least one example of a local business for each of the main forms of organization.

Type of Organization

Example of a Local Business

Sole Proprietorship:	_____
General Partnership:	_____
Limited Partnership:	_____
C-corporation:	_____
S-corporation:	_____
Limited Liability Company:	_____

Use your knowledge of local businesses to develop a list of examples for each type of ownership)

- Choose the owner of a local business – it can be someone from your family who owns a business. Briefly interview them about the form of organization of their business. Ask them questions such as:

- What is the form of organization for your business?
- What is the main reason you chose this form of organization?
- What do you think is the biggest advantage of this form?
- What do you think is the biggest disadvantage of this form?
- Who did you talk to for advice before you selected this form of business organization?

Write a 1- to 2-page paper that summarizes your interview. Please include a brief description of the business. Also, include your thoughts into your paper: for example, do you agree with the choice of organization?; What other type of organization might be appropriate for this business?; What did you learn from this interview....

Forms of Business Organization- Student Driven Learning Activity

Divide into groups and develop an interactive presentation through skit, ppt, charts/diagrams, etc... about one of the types of business organizations. Present this business type to the group without giving away the name or type and see if they can properly identify the business organization.

Forms of Organization- Additional Reading

A house should be built on a strong foundation so that it will last for years to come. If the foundation is weak, the house may fall down. If the foundation is solid, the house will not only last for years, but you can add rooms onto that house over time as your goals change.

The same thing goes for a business – it needs a solid foundation that allows it to survive and possibly grow to meet future needs. That foundation is called the “form of organization” or “form of ownership”. There are 6 primary forms of business organization that allow businesses to survive and grow over time:

- Sole Proprietorship
- General Partnership
- Limited Partnership
- C-corporation
- S-corporation
- Limited Liability Company (LLC)

Now for the big question, “which is the best form of organization for my business?” The answer is, “it depends on three main factors.” Those three factors are:

- Ease of transfer of ownership to others
- Taxation of the business’ profits
- Liability (risk) that the business faces.

Ease of transfer of ownership is important for businesses that want to continue into the future. Many family businesses are passed from one generation to the next. With certain forms of organization this transfer is complicated; with others it is very easy. The three main methods of transferring the ownership of a business from one person to another are:

- Purchasing the business from the current owner
 - You may purchase the entire business or a percentage of the business
- Giving the ownership of the business to others as a gift
- Inheriting the ownership of the business at the death of the current owner.

Each of these methods can be effective, but they will have different tax implications. More importantly, some of these methods of transferring the ownership of a business are much easier than others. We will talk about these differences later. Let’s look at Greta’s Green Grocery for a minute. If she only wants to operate the business for the next 5 years and then close it down, she will not have to be concerned with the ease of transfer – she’ll simply sell the assets. But, what if Greta wants to pass the business to her niece, Emily? Now she must think about which form of organization will allow her to transfer the business to Emily in the easiest, most effective manner.

Most people do not like to pay income taxes, although if you think about it, you only pay income taxes when you make money! So paying income taxes is not a bad thing. But you don't want to have to pay more than you have to. Most forms of business organization are taxed at the owner's personal income tax rate. This is called "pass-through taxation" – the profits literally "pass through" to the owner's personal income tax statement. The other forms of ownership are taxed at the "corporate income tax rate" – in most cases the corporate income tax rates are higher than the personal income tax rate. One major concern that business owners have is something called "double taxation". This is a situation where some of the profits of the corporation are taxed at both the corporate tax rate and the owner's personal tax rate.

The last main factor in choosing a form of organization is liability. Liability is a term that means you are responsible for any of your actions that might harm others. Some forms of organization have "unlimited liability". Unlimited liability means that the business assets AND the personal assets of the owner (houses, cars, etc.) may be sold to pay for any damages caused by the owner's business. In the case of a major lawsuit, the owner may have to sell all of the business assets, and then have to sell some of his/her personal assets to come up with enough cash to pay the damages. Some forms of organization provide "limited liability". This means that only the business assets can be used to pay the damages – but the owner's personal assets do not have to be sold to pay damages. In Greta's case, this would mean that she might have to sell the business assets (freezers, refrigerators, etc.), but not her house and car. But please understand that the forms of organization that offer limited liability do not always protect your personal assets – that's why every business needs liability insurance.

Now, let's describe the main forms of organization.

Sole Proprietorship

A sole proprietorship is owned and managed by one person. There may be several employees, but that one person owns all of the business' assets and makes all of the business decisions. The owner has full control of the business and gets all of the profits of the business. However, the owner also faces all of the risk (liability) associated with the business – he/she has unlimited liability, which means his/her personal assets are at risk because of the business.

This is the easiest form of organization to start. All you have to do is give your business a name, purchase any required business licenses or permits, and open the doors to your business. There is very little cost to start a sole proprietorship. Easy and low start-up costs – these are the two reasons that over 70% of the businesses in the US are sole proprietorships. Another reason is that the earnings of the business are taxed at the owner's personal income tax rate (which is usually lower than the corporate income tax rates).

The main disadvantages of a sole proprietorship are that it has unlimited liability, it is hard to transfer the business to someone else, and it is harder to get access to resources (such as loans). Transferring ownership of a sole proprietorship requires that you dissolve the sole proprietorship

(end its life). If the owner wants to bring in a business partner, he/she has to change from a sole proprietorship to a partnership or a type of corporation – that’s because a sole proprietorship is owned by one person, no more than that. The last disadvantage is that it is harder to get access to resources because there is only one owner. If there were 2 or 3 owners, now you can “pool” their assets together, but you can’t do that with just one person.

Partnerships

Partnerships are very similar to sole proprietorships, except that there is more than one owner. These are very simple to start, they have low start-up costs, they have unlimited liability, and the profits are taxed at the owners’ personal tax rates – just like sole proprietorships. Also, it is relatively difficult to transfer the ownership to people other than the existing owners – if you want to add new partners you may have to dissolve the existing partnership and start over.

The main difference is that there is more than one owner, and that means there can be more than one person making the decisions for the business. This can lead to arguments between the owners.

There are a couple of other things to know about partnerships. First, because there are two or more owners, they can pool their resources rather than relying on just one person’s resources. This makes it easier to have a larger business than with a sole proprietor. The second thing is that each partner is responsible for the other partner’s actions. This means that if your business partner makes a mistake, you are personally responsible for the damages. For example, assume that Greta and Emily form a partnership. One day, Emily doesn’t properly store the produce. That afternoon, some of the customers get sick from eating this produce – they decide to sue the entire business to cover their medical costs. In this case, Greta’s personal assets may have to be sold to pay the damages, even though it was Emily’s mistake!

There are two main types of partnerships – General Partnerships and Limited Partnerships. A General Partnership is what we’ve described already – more than one person, unlimited liability, and so on. In a Limited Partnership, at least one partner is a “limited partner” or a “silent partner”. Silent partners simply contribute resources to the business – such as money, land, equipment – but they have absolutely no voice in the management decisions. So they actually are “silent” when it comes to the management of the business. Silent partners have limited liability – the only thing they can lose in a liability lawsuit or bankruptcy is the value of the resources they contributed to the business. For example, let’s assume that Greta’s uncle, Greg, is a silent partner in the grocery. Greg contributed the land and building to the business. In the event of a lawsuit, the only things that Greg might lose are the land and the building. No one can force Greg to sell his personal assets to cover the damages. But Greta and Emily, who are not silent partners, may lose some of their personal assets. Please note that a silent partner can never make any management decisions for the partnership. If he/she does make some management decisions, he/she is no longer a silent partner and his/her personal assets are now at risk.

Corporations

Corporations are more formal than sole proprietorships and partnerships. You typically need legal help in establishing a corporation – that means you have to hire a lawyer, and that costs money. To establish a corporation you need to have corporate by-laws (rules of operating the business) and articles of incorporation (legal documents describing the business) that are filed with the State Corporation Commission. So forming a corporation is harder and more expensive than forming a sole proprietorship or partnership.

Corporations have an “unlimited lifetime” – that means that they continue to exist even when some of the owners die or leave the business. This is not true for sole proprietorships or partnerships. All you need to do to be an owner of a corporation is own “shares” of the corporation’s “stock”. One stock is equivalent to one share of the ownership of the corporation. If you want to be an owner of John Deere, all you have to do is purchase one of more shares of the John Deere stock - it’s that simple! And once you own stock you can sell it, give it away, or you can leave it to your heirs as an inheritance. This makes it very easy to transfer the ownership of a corporation to other owners. If Greta formed her store as a corporation, she can make Emily a co-owner by giving her some shares or selling her some shares. Greta can even leave the remaining shares of her stock in the business to Emily in her will. One of the main reasons owners choose to form a corporation is that it is very easy to transfer the ownership.

Another reason that owners like to form their business as a corporation is that it provides limited liability to the owners (shareholders). In most cases, a shareholder of a corporation can only lose the value of his/her investment in the stock of the corporation. For example, assume that you own \$1,000 of stock in John Deere. If John Deere were to be sued or go bankrupt, the maximum that you would lose is your \$1,000 of stock – no one can come after your personal assets. However, do NOT rely on this to protect your personal assets – every business owner needs liability insurance to fully protect his/her personal assets.

Corporations also allow owners to gain access to more resources than sole proprietorships and partnerships. If a corporation wants to generate more cash so that they can buy new equipment, they can simply sell more shares of the company. This raises cash that can be used for expanding the business or paying off loans.

Taxation of corporations is different than for sole proprietorships and partnerships. For most corporations, the earnings of the company are taxed at the corporate tax rate, which is usually higher than the personal tax rate. Further, if the corporation decides to pay some of the after-tax profits to its shareholders as a reward for investing in the company, these “dividend” payments are taxed again at the personal tax rate. This is called “double taxation”.

There are two main types of corporations for most business owners: C-corporations and S-corporations. A C-corporation is a business that has no limits on who can be an owner. The profits of a C-corporation are taxed at the corporate tax rate. An S-corporation has limitations on how

many people can be an owner of the business (no more than 75). S-corporations are used by many family-owned businesses so that they can keep the ownership of the company to members of the family. Hence, S-corporations are sometimes called “closely-held corporations” because the ownership is held within the family. The profits of an S-corporation are taxed at the owner’s personal tax rate. Regardless of which type of corporation you choose, you can form a corporation with as little as one owner.

Limited Liability Companies (LLC)

Limited Liability Companies (LLCs) are a combination between corporations and partnerships. As the name states, LLCs offer the owners a form of limited liability (to protect their personal assets). This protection is limited to the value of their ownership in the business. Where owners of a corporation are called shareholders, the owners of an LLC are called “members” – but in reality there is not much difference between shareholders and members.

LLCs are very flexible. Owners can structure an LLC so that it looks and acts like a C-corporation, or like an S-corporation, or like a partnership or sole proprietorship. Most LLCs are set up so the profits are taxed at the owner’s personal tax rate. This allows the owner(s) to avoid double taxation.

To be honest with you, there is not a very big difference between a C-corporation, an S-corporation, and an LLC for most small businesses. They each provide limited liability, have an unlimited lifetime, and can easily be transferred to other owners. The primary difference between these three forms of business is the method in which the profits are taxed.

Please see the following table for a side-by-side comparison of the main forms of business organization.

What about Greta? Which form is best for her green grocery? The answer to that depends on her goals. Here’s a brief look at her decision:

If she only wants to operate the business on her own for a few years and has no interest in transferring the ownership to someone else:

A sole proprietorship might be a good choice. It is easy to set up, it doesn’t cost much money to set-up, and she is in complete control of the business. The main disadvantage is that she will face unlimited liability – that means her personal assets are at risk. But she can reduce that risk by having liability insurance.

She could form a corporation (C or S) or an LLC in this case. This would be more costly, but might provide a little more liability protection. It also makes it easier to transfer ownership if she changes her mind in the future.

If she wants to operate the business with Emily as a co-owner and manager:

Because there is more than one owner, we can rule out a sole proprietorship. If both Greta and Emily are making management decisions they cannot be “silent partners” – so that rules out a

limited partnership. But any of the remaining forms would be appropriate. The general partnership would be the easiest and lowest cost organization to set up; however, it would have unlimited liability and it would be relatively difficult to bring in other partners.

They could form a corporation (C or S) or an LLC in this case as well. This would be more costly, but might provide a little more liability protection. It also makes it easier to bring in new owners in the future. It also makes it much easier for Greta to turn the entire business over to Emily when Greta decides she wants to retire – she can either sell her shares in the business to Emily, or gift them to her.