Differences of partnerships, c corporations and s corporations to include tax adv...

Business, Company

A partnership is an agreement in which two or more persons combine their resources in a business with a view to making a profit. In order to establish the terms of the partnership and to protect partners in the event of a disagreement or dissolution of a partnership, a partnership agreement should be drawn up. Partners share in the profits according to the terms of the agreement. Its advantages are: ease of formation, low start-up costs, additional sources of investment capital, possible tax advantages, limited regulation, broader management base. Its disadvantages are: unlimited liability, divided authority, difficulty in raising additional capital, hard to find suitable partners, possible development of conflict between partners, partners can legally bind each other without prior approval, lack of continuity.

A C Corporation also goes by the name of " A profit corporation." In A C Corporation, income taxes are paid by both the corporation and shareholders. If the C Corporation incurred any losses, those losses remain the property of the C Corporation and made the responsibility of the shareholder. Even in the case of bankruptcy, the owners of the C Corporation are not liable for any debts of the business.

Like the C Corporation, the S Corporation is named after the Internal Revenue Code section that allows it. An S Corporation is a corporation which has elected for its profits to be taxed in the manner of an unincorporated entity, meaning there is no double taxation. Like C Corporations, not all corporations can opt to become an S Corporation. Those applying for the status of S corporation are typically small businesses, such as retail,

consultants, partnerships, sales driven organizations, family businesses or companies maintaining

depreciating assets. Due in part to the factor of depreciating assets, an S Corporation's passive income does not exceed 25 percent of the total income, such as annuities, dividends, royalties or other sources. Subchapter S is ideal for smaller companies. These companies do not typically need to worry about shareholders as their number of shareholders is typically significantly less than the number of shareholders that a C Corporation has. An S Corporation typically has less than 75 shareholders, all of whom agree to incorporate the business under an " S" corporation. The S Corporation has the significant advantage of avoiding double taxation. Another advantage of the S Corporation is that it does not pay federal taxes. Business profits pass through to individual stockholders, who then must report them on their individual tax returns. This is done when the corporation sends once a year to shareholders a K-1 Internal Revenue Tax Form. The form reports the distribution of any income to shareholders, and any loss passed onto the shareholder, from the corporation. It is then the shareholder's responsibility to include this distribution of income information in the filing of their own personal taxes. Likewise, if there are losses, the shareholders can use those losses as a deduction on their individual tax returns.

Overall, tax rates applicable to many individuals in a C Corporation are lower than the rates that would apply to an S corporation even when the employees or owners of the two different corporations are at the same income level. Also, there are tax-free fringe benefits for shareholder-

employees belonging to a C Corporation. In this situation fringe benefits include such things as pension plan contributions and health care availability. The corporation can make pension fund contributions or buy health insurance for employees without having those benefits taxed. These pension fund and health insurance expenditures are actually tax deductions for the corporation.

A C Corporation is not confined by the rules of issuing shares the same way that an S Corporation is limited. C Corporations can have a great deal more shareholders than an S Corporation and the shares that are issued can be of varying classes. Furthermore, shareholders are not required to be U. S. Citizens or permanent residents as is the requirement to own stock under an S Corporation. When this source of equity capital is not restricted, the C Corporation has greater opportunities for more rapid growth. C Corporations are also easier to manage estate planning under.

One of the first things that those forming an S Corporation find most appealing is that those with S Corporation status are not required to pay both corporate and individual income taxes. However it is only fair to note that because the shareholders are not subject to double taxation, they may end up paying a higher personal income tax rate. When total taxes are considered over the course of the year, both on the corporate and on the individual level, those belonging to an S Corporation almost always end up paying fewer income taxes.

Employment tax rules are also favorable under an S Corporation versus a C Corporation. In Corporations such as the S Corporation where shareholder-employees are in smaller numbers, it is possible for all of the corporation's profits to be extracted in the form of a salary that is paid. This means that the corporation can pay out its profits in the form of wage increases or bonuses at the end of the year, making the taxable amount for income zero. When income is zero there is no need to pay income taxes. Employee-shareholder wages are subject to employee taxes but payments taken out of profit and distributed to shareholders are not subject to employment taxes.

Both the C Corporation and the S Corporation offer the same limited liability protection for shareholders/owners. By incorporating under either of these two structures you will still be protecting yourself from being personally responsible for the debts and liabilities of the business. The process of incorporating (for example, forming the appropriate documents required by the state) is the same regardless of whether you decide to have your business be an S or a C Corporation.

Both types of corporations have shareholders, directors and officers. In both cases the shareholders are the owners of the company and these owners are responsible for the election of the board of directors. Organizationally the two corporations are also the same in that the board of directors oversees and directs the affairs of the company and the directors elect officers to manage the daily affairs of the business. Both types of corporations are required to follow the same formalities internally and externally such as adopting bylaws, issuing shares of stock, and annual and shareholder

meetings as well as the minutes of these meetings. They are also required to file the same appropriate annual reports required by each state and the fees associated with these reports.

References

http://www. laughlinusa. com/incorporating-about. asp