Limited Liability Companies

The limited liability company (LLC) is a distinct business entity that combines the corporate advantage of limited liability protection with "pass-through" taxation, the method of taxation afforded to both general partnerships and S corporations.

Like corporations, LLCs come into existence after making a filing with the appropriate state body, typically the Secretary of State, and paying the necessary state filing fees. The LLC formation documents are typically called articles of organization or a certificate of organization.

In terms of taxation, the LLC's income is not taxed at the entity level as is that of a C corporation. While the LLC does complete a tax return, the income or loss of the LLC as shown on this return is passed through the LLC and is reported on the owners' individual tax returns. The LLC's owners then pay taxes on the LLC's profits at the individual tax level. LLCs can elect with the Internal Revenue Service (IRS) to be taxed like a C corporation, but this is not overly common.

Other advantages of LLCs include:

- Members are typically not held personally responsible for the debts and liabilities of the company.
- Forming an LLC can help establish credibility for a new business with potential customers, employees, vendors, and partners.
- There are generally no restrictions on the number of members allowed.
- LLCs have flexibility in structuring the management of the company.
- LLCs do not require as much annual paperwork or have as many formalities as corporations and S corporations.

Some disadvantages of LLCs include:

- LLCs are more expensive to form than sole proprietorships and general partnerships.
- LLCs face more ongoing requirements, such as state annual report filings, than sole proprietorships and general partnerships.
- Ownership is typically harder to transfer than with a corporation.
- Because the LLC is a newer business structure, there is not as much case law to rely on for determining precedent.

Regarding the ownership of an LLC, the owners are called members. Members are analogous to shareholders in a corporation or partners in a partnership, depending on how the LLC is structured. Members will more closely resemble shareholders if the LLC utilizes a manager or managers because the members will not directly participate in the management of the LLC. If the LLC does not utilize managers, then the members will more closely resemble partners because they will have a direct say in the decision-making of the company. An LLC must specify at the time of formation whether it will be managed by members or managers.

A member's ownership of an LLC is represented by "membership interest," just like a partner's interest in a partnership or a shareholder's shares of stock in a corporation.

When evaluating whether the LLC is the right business structure for your particular business, it is advisable to first determine the goals of your business, and then to assess the advantages and potential disadvantages of the different business structures in relation to those goals. You may also wish to seek the advice of an attorney or accountant.

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