NACM Northwest

Informational Brief

Business Structures

SOLE PROPRIETORSHIP

A sole proprietor is the simplest form of business in which one individual conducts the business. The vast majority of small businesses start out as sole proprietorships. Sole proprietors own all the assets of the business and the profits generated by it. They also assume complete responsibility for any of its liabilities or debts. In the eyes of the law and the public, you are one in the same with the business.

Advantages of a Sole Proprietor

- Easiest and least expensive form of ownership to organize.
- Sole proprietors are in complete control, and within the parameters of the law, may make decisions as they see fit.
- Sole proprietors receive all income generated by the business to keep or reinvest.
- Profits from the business flow directly to the owner's personal tax return.
- The business is easy to dissolve, if desired.

Disadvantages of a Sole Proprietor

- Sole proprietors have unlimited liability and are legally responsible for all debts against the business. Their business and personal assets are at risk.
- May be at a disadvantage in raising funds and are often limited to using funds from personal savings or consumer loans.
- May have a hard time attracting high-caliber employees or those that are motivated by the opportunity to own a part of the business.
- Some employee benefits such as owner's medical insurance premiums are not directly deductible from business income (only partially deductible as an adjustment to income.)

Federal Tax Forms for Sole Proprietorship (only a partial list and some may not apply)

- Form 1040: Individual Income Tax Return
- Schedule C: Profit or Loss from Business (or Schedule C-EZ)
- Schedule SE: Self-Employment Tax
- Form 1040-ES: Estimate Tax for Individuals
- Form 4562: Depreciation and Amortization
- Form 8892: Expenses for Business Use of your Home
- Employment Tax Forms

PARTNERSHIPS

In a partnership, two or more people share ownership or a single business. Like proprietorships, the law does not distinguish between the business and its owners. The partners should have a legal agreement that sets forth how decisions will be made, profits will be shared, disputes will be resolved, how future partners will be admitted to the partnership, how partners can be bought out, and what steps will be taken to dissolve the partnership when needed. Yes, it's hard to think about a breakup when the business is just getting started, but many partnerships split up at crisis times, and unless there is a defined process, there will be even greater problems. They also must decide up-front how much time and capital each will contribute, etc.

Advantages of a Partnership

- Partnerships are relatively easy to establish; however time should be invested in developing the partnership agreement.
- With more than one owner, the ability to raise funds may be increased.
- The profits from the business flow directly through to the partners' personal tax returns.
- Prospective employees may be attracted to the business if given the incentive to become a partner.
- The business usually will benefit from partners who have complimentary skills.

Disadvantages of a Partnership

- Partners are jointly and individually liable for the actions of the other partners.
- Profits must be shared with others.
- Since decisions are shared, disagreements can occur.
- Some employee benefits are not deductible from business income on tax returns.
- The partnership may have a limited life; it may end upon the withdrawal or death of a partner.

Types of Partnerships that should be considered:

1. **General Partnership**
   Partners divide responsibility for management and liability as well as the shares of profit or loss according to their internal agreement. Equal shares are assumed unless there is written agreement that states differently.
2. **Limited Partnership and Partnership with limited liability**
   Limited means that most of the partners have limited liability (to the extent of their investment) as well as limited input regarding management decisions, which generally encourages investors for short-term projects or for investing in capital assets. This form of ownership is not often used for operating retail or service businesses. Forming a limited partnership is more complex and formal than that of a general partnership.
3. **Joint Venture**
   Acts like a partnership, but is clearly for a limited period of time or a single project. If the partners in a joint venture repeat the activity, they will be recognized as an ongoing partnership and will have to file as such as well as distribute accumulated partnership assets upon dissolution of the entity.

Domestic Limited Liability Partnership

To form a domestic limited liability partnership, an application for registration and a non-refundable $50 processing fee must be submitted to Business Registry. Before a limited liability partnership is filed, the name is checked for availability. The name must be distinguishable from other active names on a Business Registry records. In addition, the name of the limited liability partnership must contain the words "Limited Liability Partnership" or the abbreviation "L.L.P." or "LLP" as the last words or letters of its name. If the name is distinguishable and the application conforms to Oregon statute, Business Registry processes the document and returns an acknowledgement to the customer.

Foreign Limited Liability Partnership

A foreign limited liability partnership must obtain authority from Business Registry to transact business in Oregon. An application for authorization and a non-refundable $50 processing fee must be submitted to Business Registry. A certificate of existence or similar document from the jurisdiction of organization must be submitted with the application form. The certificate or similar document must be dated within 60 days of the date of the application. Before an application for authorization is filed, the name is checked for availability. The name must be distinguishable from other active names on Business Registry records. In addition, the name of the limited liability partnership must contain the words "Limited Liability Partnership" or the abbreviation "L.L.P." or "LLP" as the last words or letters of its name. If the name is distinguishable and the application conforms to Oregon statute, Business Registry processes the document and returns and acknowledgment to the customer.

Domestic and foreign limited liability partnerships are regulated by the Oregon Revised Partnership Act, ORS Chapter 67.

Federal Tax Forms for Partnerships (only a partial list and some may not apply)

- Form 1065: Partnership Return of Income
- Form 1065 K-1: Partner's Share of Income, Credit, Deductions
- Form 4562: Depreciation
- Form 1040: Individual Income Tax Return

- Schedule E: Supplemental Income and Loss
- Schedule SE: Self Employment Tax
- Form 1040-ES: Estimated Tax for Individuals
- Employment Tax Forms

CORPORATION

A corporation is a legal entity created under Oregon Statute by submitting articles of incorporation with Business Registry. A corporation is owned by its shareholders, in whose names the shares are registered in the records of the corporation. The articles of incorporation must state how many shares the corporation has authority to issue.

A corporation acts as a single entity. It exists separately from its owners, and continues to exist even though the shareholders may change. As a separate entity, a corporation must file its tax returns. It may own property, sue, and be sued.

A corporation is managed by a board of directors. Except for the initial board, the shareholders generally select the directors. The number of directors is determined by the articles of incorporation or the bylaws. The directors must elect the president and secretary and adopt bylaws. The board may elect or appoint other officers, or the bylaws may prescribe how other officers are selected. The same person can hold two or more offices.

A corporation must have a registered agent in Oregon whose street address is the registered office. When a corporation is sued, the legal papers are served on the registered agent. Thus, it is necessary that the registered office have a street address. A registered agent can be an individual or a legal entity.

The three common types of corporations filed in Oregon are business corporations, nonprofit corporations, and professional corporations. Business and professional corporations are for-profit corporations. A nonprofit corporation is formed for any lawful purpose except for financial profit. A professional corporation is a for-profit corporation formed for the purpose of providing one or more specific types of professional service. All the shareholders of the professional corporation must be licensed to render one of the professional services.

Corporations formed under Oregon statute are "domestic" corporations. Those formed under the laws of other states, but transacting business in Oregon, are "foreign" corporations.

Domestic Corporation

To form a domestic corporation in Oregon, articles of incorporation and a non-refundable $50 processing fee must be submitted to Business Registry. Before articles of incorporation are filed, the name is checked for availability. The name must be distinguishable from other active names on Business Registry records. If the name is distinguishable and the articles conform to Oregon statute, Business Registry processes the document and returns an acknowledgement to the customer.

Once the existence of the corporation is established, an organizational meeting of the board of directors is generally held to adopt bylaws and elect officers. The bylaws of the corporation may contain any provisions to regulate and manage the affairs of the corporation consistent with statutes and the articles of incorporation.

Note: The Corporation Division does not have a separate filing for an S corporation. The S designation is a federal tax designation. A business corporation that meets the Internal Revenue Service (IRS) requirements for S corporation status can apply for federal tax status as an S corporation by filing Form 2553, "Election by a Small Business Corporation," with IRS.

Foreign Corporation

A foreign corporation must obtain authority from Business Registry to transact business in Oregon. An application of authority, including the name and address of its Oregon registered agent and a non-refundable $50 processing fee must be submitted to Business Registry. A certificate of existence or similar document from the jurisdiction of incorporation must be submitted with the application form. The certificate or similar document must be dated within 60 days of the date of application. Before an application of authority is filed, the name is checked for availability. The name must be distinguishable from other active names on Business Registry records. If the name is distinguishable and the application conforms to Oregon statute, Business Registry processes the document and returns an acknowledgment to the customer.

Domestic and foreign business corporations are regulated by the Oregon Business Corporation Act, ORS Chapter 60. Domestic and foreign nonprofit corporations are regulated by the Oregon Nonprofit Corporation Act, ORS Chapter 65. Domestic and foreign professional corporations are regulated by the Oregon Professional Corporations Act, ORS Chapter 58.

Advantages of a Corporation

- Shareholders have limited liability for the corporation's debts or judgments against the corporations.
- Generally, shareholders can only be held accountable for their investment in stock of the company.
  Note: However, officers can be held personally liable for their actions, such as the failure to withhold and pay employment taxes.)
- Corporations can raise additional funds through the sale of stock.
- A corporation may deduct the cost of benefits it provides to officers and employees.
- Can elect S corporation status if certain requirements are met. This election enables company to be taxed similar to a partnership.

Disadvantages of a Corporation

- The process of incorporation requires more time and money than other forms of organization.
- Corporations are monitored by federal, state and some local agencies, and as a result may have more paperwork to comply with regulations.
- Incorporating may result in higher overall taxes. Dividends paid to shareholders are not deductible from business income; thus it can be taxed twice.

Federal Tax Forms for Regular or "C" Corporations (only a partial list and some may not apply)

- Form 1120 or 1120-A: Corporation Income Tax Return
- Form 1120-W: Estimated Tax for Corporation
- Form 8109-B: Deposit Coupon
- Form 4625: Depreciation
- Other forms as needed for capital gains, sales of assets, alternative minimum tax, etc.

Subchapter S Corporations

A tax election only; this election enables the shareholder to treat the earnings and profits as distributions and have them pass through directly to their personal tax return. The catch here is that the shareholder, if working for the company, and if there is a profit, must pay him/herself wages, and must meet standards of "reasonable compensation." This can vary by geographical region as well as occupation, but the basic rule is to pay yourself what you would have to pay someone to do your job, as long as there is enough profit. If you do not do this, the IRS can reclassify all of the earnings and profit as wages, and you will be liable for all the payroll taxes on the total amount.

F**ederal Tax Forms for "S" Corporations (only a partial list and some may not apply)**

- Form 1120S: Income Tax Return for S Corporation
- 1120S K-1: Shareholder's share of Income, Credit, Deductions
- Form 4625: Depreciation
- Employment Tax Forms
- Form 1040: Individual Income Tax Return
- Schedule E: Supplemental Income and Loss
- Schedule SE: Self-Employment Tax
- Form 1040-ES: Estimated Tax for Individuals
- Other forms as needed as capital gains, sale of assets, alternative minimum tax, etc.

Informational Brief

Business Structures

Limited Liability Company (LLC)

The LLC is a relatively new type of hybrid business structure that is now permissible in most states. It is designed to provide the limited liability features of a corporation and the tax efficiencies and operational flexibility of a partnership. Formation is more complex and formal than that of a general partnership.

The owners are members, and the duration of the LLC is usually determined when the organization papers are filed. The time limit can be continued, if desired, by a vote of the members at the time of expiration. LLC's must not have more than two of the four characteristics that define corporations: Limited liability to the extent of assets, continuity of life, centralization of management, and free transferability of ownership interest.

Federal Tax Forms for LLC

Taxed as partnership in most cases; corporation forms must be used if there are more than 2 of the 4 corporate characteristics, as described above.

What is the difference between a Corporation and a Limited Liability Company?

A Corporation is a separate legal entity. It can sue and be sued, buy and sell property, etc. A Limited Liability Company is an unincorporated association consisting of one or more members. LLC's are managed by managers or their members.

Assumed Business Name Registration

The main reason to register your business name is to tell the public (and other businesses) who is doing business under that name.

A business name must be registered with the Corporation Division as an assumed business name if the "real and true" name of each person who is carrying on the business is not conspicuously disclosed to the public in the business name. Each person's "real and true" name must include first name, middle initial and last name. Nicknames are not "real and true" names and must be registered as assumed business names. If there are words that suggest additional owners, such as "company" or "associates", the business name must be registered.

A business name that includes the "real and true" names of all owners' may also be registered, but the registration is optional. A corporation, limited liability company, limited liability partnership, or limited partnership does not need to register its name as an assumed business name, unless the entity wants to use the name without the entity type designation.

If a person transacts business with an unregistered assumed business name, he or she may not have standing in court to pursue or defend legal actions, and may find it difficult to do business, for example, getting licenses, opening bank accounts, and entering into contracts.

Information provided by: Oregon Secretary of State Corporation Division (SOS) (www.filinginoregon.com)

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