

Limited Liability Companies (LLCs) versus S Corporations (S Corps)

| Similarities | |
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| Limited liability protection | <ul style="list-style-type: none"> • With both, owners are typically not personally responsible for business debts and liabilities. |
| Separate entities | <ul style="list-style-type: none"> • Both are separate legal entities created by a state filing. |
| Pass-through taxation | <ul style="list-style-type: none"> • Both are typically pass-through tax entities, and while S corps must file a business tax return, LLCs only file business tax returns if the LLC has more than one owner. • With pass-through taxation, no income taxes are paid at the business level. Business profit or loss is passed-through to owners' personal tax returns. Any necessary tax is reported and paid at the individual level. |
| State requirement for formation and on-going operation | <ul style="list-style-type: none"> • Both are subject to state-mandated formalities, such as filing biennial reports, communicating changes, and paying the necessary fees. |

| Differences | |
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| Ownership | <ul style="list-style-type: none"> • The IRS restricts S corp ownership, but not that of LLCs. IRS restrictions include the following: <ul style="list-style-type: none"> ○ LLCs can have an unlimited number of members; S corps can have no more than 100 shareholders (owners). ○ Non-U.S. citizens/residents can be members of LLCs; S corps may not have non-U.S. citizens/residents as shareholders. ○ S corps cannot be owned by C corporations, other S corps, LLCs, partnerships or many trusts. This is not the case for LLCs. ○ LLCs are allowed to have subsidiaries without restriction. |
| Stock | <ul style="list-style-type: none"> • S corps can sell stock. • LLCs can only sell interest in the company. |
| Ongoing formalities | <ul style="list-style-type: none"> • S corps face more extensive internal formalities. LLCs are recommended, but not required, to follow internal formalities. <ul style="list-style-type: none"> ○ Required formalities for S corps include: Adopting bylaws, issuing stock, holding initial and annual director and shareholder meetings, and keeping meeting minutes with corporate records. ○ Recommended formalities for LLCs include: Adopting an operating agreement, issuing membership shares, holding and documenting annual member meetings (and manager meetings, if the LLC is manager-managed), and documenting all major company decisions. |
| Management | <ul style="list-style-type: none"> • Owners of an LLC can choose to have members (owners) or managers manage the LLC. When members manage an LLC, the LLC is much like a partnership. If run by managers, the LLC more closely resembles a corporation; members will not be involved in the daily business decisions. • S corps have directors and officers. The board of directors oversees corporate affairs and handles major decisions but not daily operations. Instead, directors elect officers who manage daily business affairs. |



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| Transferability of ownership | S corp stock is freely transferable, as long as IRS ownership restrictions are met. LLC membership interest (ownership) typically is not freely transferable—approval from other members is often required. |
| Appeal to investors | S corps are generally more appealing, not only due to the ability to issue stock, but also because S corps have a more rigid management structure and more extensive reporting requirements. |
| Self-employment taxes | <ul style="list-style-type: none">• S corps may have preferable self-employment taxes compared to the LLC because the owner can be treated as an employee and paid a reasonable salary. FICA taxes are withheld and paid on that amount. Corporate earnings after payment of the salary may be able to be treated as unearned income that is not subject to self-employment taxes. |
| Other taxes | <ul style="list-style-type: none">• An LLC is either recognized on the Schedule C of an individual return or as a partnership if multiple partners, whereas an S corp always must file an 1120S.• An individual owner of an LLC does not pay unemployment or disability taxes, but that also means that the owner is not entitled to state unemployment or disability benefits. |

For more information about tax issues, please consult your accountant or tax adviser.