S-Corp Election

What is it and does it make sense for your business?

When forming a business, one of the key decisions you'll face is choosing the right legal and tax structure. While LLCs and corporations are the most common entity types, **both LLCs and Corporations can opt into a special tax status known as an S-Corporation election by filing with the IRS**. An S-Corp isn't a separate entity type, but rather a tax designation that allows profits to "pass through" to the owners' personal tax returns, avoiding double taxation faced by traditional C-corporations. For LLCs, electing S-Corp status can help reduce self-employment taxes by allowing owners to split income between salary and profit distributions. For C-corps, the S-Corp election can simplify tax treatment for closely held businesses with 100 or fewer U.S. shareholders. However, strict requirements apply , such as limiting ownership to U.S. individuals and permitting only one class of stock. The chart below breaks down the key differences between LLCs, C-Corps, and entities that have elected S-Corp status to help you decide what structure makes the most sense for your business.

FEATURE	LLC	C-CORP	LLC (ELECTING S-CORP)	C-CORP (ELECTING S-CORP)
LEGAL STRUCTURE	Flexible entity governed by an operating agreement	Separate legal entity with formal corporate governance	Same LLC structure, taxed as S-Corp	Same C-Corp structure, taxed as S-Corp
OWNERSHIP	Members (no limit; individuals or entities)	Shareholders (no limit; any entity or individual)	Max 100 shareholders; U.S. citizens/residents and certain trusts only	Max 100 shareholders; U.S. citizens/residents and certain trusts only
MANAGEMENT	Member- or manager-managed	Board of Directors with officers	Same as LLC	Same as C-Corp
TAXATION	Pass-through by default (profits taxed at member level)	Double taxation (corporation taxed, then shareholders taxed on dividends)	Pass-through taxation (profits/losses taxed once at owner level)	Pass-through taxation (profits/losses taxed once at owner level)
SELF-EMPLOYMENT TAX	Members pay self-employment tax on all profits	Not applicable to corporation (corporation pays employer taxes; shareholders do not pay self-employment tax)	**Only the owner's salary** is subject to self-employment tax; **remaining profits (distributions)** are not	Same as LLC with S-election: only salary is subject to self-employment tax; distributions are not

PROFIT DISTRIBUTION	Flexible; does not need to be proportional to ownership	Must be proportional to share ownership	Must be proportional to ownership	Must be proportional to ownership
FORMALITIES	Minimal: no board, minutes, or bylaws required	Strict: must hold annual meetings, adopt bylaws, keep minutes	Fewer formalities unless state requires more	Same as C-Corp: full corporate formalities required
RAISING CAPITAL	Harder to raise VC or institutional funding	Easier to raise capital through equity investment	Limited due to S-Corp shareholder and stock restrictions	Limited due to S-Corp shareholder and stock restrictions
FRINGE BENEFITS	Limited deductions for owners	Can deduct many fringe benefits for employees and shareholder-employees	Limited fringe benefits for 2%+ owner-employees	Limited fringe benefits for 2%+ shareholder-employees
CLASSES OF OWNERSHIP	Unlimited flexibility; can customize membership rights	Unlimited classes of stock (e.g., common, preferred)	**Only one class of stock allowed** (voting/non-voting differences OK)	**Only one class of stock allowed** (voting/non-voting differences OK)
BEST FOR	Small businesses needing flexibility and fewer formalities	Startups and high-growth businesses seeking outside investment	Small business owners looking to reduce payroll taxes and retain pass-through treatment	Closely held businesses seeking pass-through tax treatment but structured as a corporation

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