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LIMITED LIABILITY COMPANY CONVERSIONS

Taking Advantage of a Tax Chameleon

Many small business owners in Florida choose a limited liability company ("LLC") when forming their business. The Treasury Department's "check the box" regulations allow LLCs to elect to be taxed as a C corporation ("C-corp"), S corporation ("S-corp"), tax partnership, or, in the case of single-member LLCs, a disregarded entity. In this sense, the LLC is a "tax chameleon," as the tax status of the LLC can be carefully selected to suit the needs of the business and its owners. Though LLCs have been around for some time, not all business owners have taken advantage, especially those who have long-standing businesses organized as corporations. Under Florida law, corporations (whether taxed as a C-corp or an S-corp) are easily afforded the opportunity to convert to an LLC without disturbing the original tax status of the entity.

Key Advantages of Converting to a Multi-Member LLC

- ☐ **Asset Protection**. Corporate stock is not protected from a business owner's personal liabilities, as a creditor may obtain ownership of the stock. Converting the corporation to a multi-member LLC protects against this possibility because a charging order is the exclusive remedy available to a creditor of an owner of a multi-member LLC interest (see LLCs and Charging Order Protection – Why Single Member LLCs Are Not Always Enough (https://ivanlawgroup.com/blog/f/llcs-and-charging-order-protection). The increased asset protection created by limiting creditors to a charging order is a significant benefit when converting to a multi-member LLC.
- ☐ **Limited Liability**. LLCs protect an owner's personal assets from business liabilities to the same extent as a corporation, which is the highest protection under Florida law.
- ☐ **Lower Maintenance**. LLCs do not require the same level of corporate formality and corporate housekeeping to maintain limited liability protection. In addition to other factors, failure to follow corporate formalities is one of the key elements in a creditor's ability to pierce the corporate veil. Piercing the corporate veil can subject the individual owners to personal liability for the company's debts.
- ☐ **Tax Considerations**. Because an LLC can elect to be taxed in various ways, the prior tax history of a converting entity will not be modified. This is especially important for entities that already operate as an S-corp or a C-corp, as the loss of the original tax status can carry significant negative tax implications.

Examples:

- ☐ **S-Corporation**. A construction business owned by multiple individuals operates as an S-corp. The owners can convert the S-corp into a multi-member LLC taxed as an S-corp, thereby creating charging order protection while maintaining the original Subchapter S election for tax purposes. Therefore, if a business owner acting as a qualifying agent is personally sued for supervising a project on the job, their business equity is protected against forced sale in the event of a judgment.
- ☐ **C-Corporation**. A physician group created years ago as a C-corp now desires to convert to a multi-member LLC in order to asset protect their business interests. The physician group can convert from the C-corp to a multi-member LLC taxed as a C-corp and still maintain their original tax status. Therefore, if a doctor is personally sued for malpractice, their equity in the company is protected against forced sale in the event of a judgment.