WHAT TYPE OF BUSINESS DO I FORM?

Publication Date: September 25, 2024

Understanding the options for starting a business is crucial! From sole proprietorships to LLCs, choosing the right legal structure impacts everything from taxes to liability to management.

The intended audience for this paper includes aspiring entrepreneurs and small business owners. It describes the options for registering a business as a legal entity, including the benefits and obstacles of each.

Sole Proprietorship[1]

A sole proprietorship is a business owned and operated by a single individual. It is the simplest form of business structure, where the owner assumes full responsibility for all aspects of the business, including debts and liabilities.

ADVANTAGES

- Simple to set up
- Complete control
- Low cost

Best for: Small, low-risk businesses

DISADVANTAGES

- Unlimited personal liability
- Harder to raise capital

Partnership[2]

A partnership is formed when two or more individuals come together to conduct business. Each partner contributes resources—whether in the form of capital, property, labor, or skills—and shares in the profits and losses based on their agreement.

ADVANTAGES

- Shared financial commitment
- Easy to establish
- Complementary skills among partners

Best for: Professional groups or businesses with multiple owners

DISADVANTAGES

- Joint liability
- Potential for disagreements

LLC[3]

A limited liability company (LLC) offers business owners protection from personal liability for their company's debts and obligations, while providing tax flexibility. The LLC is a separate legal entity, allowing owners to avoid the double taxation that typically applies to corporations.

ADVANTAGES

- Limited liability protection
- Exclusive business name
- Flexibility in management and taxation

DISADVANTAGES

- Self-employment taxes
- Limited life in some states

- Avoids double taxation

Best for: Small to medium-sized businesses seeking liability protection

C Corp[4]

A corporation (c corp) is established when individuals, known as shareholders, invest money or property in exchange for ownership through capital stock. The corporation itself becomes a separate legal entity, distinct from its owners.

ADVANTAGES

- Limited liability for owners
- Easier to raise capital through stock
- Perpetual existence

Best for: Larger businesses or those planning to scale significantly

DISADVANTAGES

- Double taxation (profits and dividends)
- Complex structure and regulations

S Corp[5]

S corps are a special type of corporation that allows income, losses, deductions, and credits to pass through to shareholders for federal tax purposes, helping avoid the double taxation faced by traditional corporations.

ADVANTAGES

- Avoids double taxation (pass-through entity)
- Limited liability for shareholders

Best for: Small businesses looking for tax savings and limited liability

DISADVANTAGES

- Ownership restrictions (no more than 100 shareholders)
- Ongoing requirements and filings
- Ineligible corporations

Nonprofit[6]

A nonprofit organization is formed to pursue goals other than profit generation. Its income is not distributed to members, directors, or officers but is instead reinvested to further the organization's mission.

ADVANTAGES

- Tax exemptions
- Grants and donations
- Limited liability

Best for: Charitable, religious, or educational organizations

DISADVANTAGES

- Strict regulations and oversight
- No profit distribution to owners

PC[7]

A professional corporation (PC) is a type of entity created under state law, allowing licensed professionals such as doctors, lawyers, architects, and accountants to form a corporation specifically for providing their professional services.

ADVANTAGES

- Limited liability for malpractice claims
- Tax benefits

DISADVANTAGES

- Not available to all professions
- Stricter regulations
- Still liable for own negligence/malpractice

Best for: Licensed professionals in regulated industries

Co-op[8]

A cooperative (co-op) is a business entity owned and controlled by the people who use its services. Profits generated by the cooperative are distributed to its members, known as user-owners, based on their usage or involvement.

ADVANTAGES

- Democratic control
- Benefits distributed to members
- Perpetual existence

Best for: Consumer-based or community-focused organizations

DISADVANTAGES

- Difficult to raise capital
- Requires significant member involvement

Sources

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2–Partnerships|IRS.gov

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PHONE NUMBER

(208) 540-4300

EMAIL

info@idahoecenter.org

ADDRESS

35 N 1st E, Suite 3, Rexburg, ID 83440