

CHOOSING THE PROPER ENTITY

Choosing the proper type of entity in business is like choosing the proper spouse in personal life. It is also critical for businesses that are newly created or in a state of transition that the business owners evaluate a set of confusing federal and state tax and legal issues and consider personal issues when deciding what type of entity their business should be.

As a practitioner we need to ask many questions, summarize the facts. Realize that we don't know what the future holds, then make a decision on the facts.

Please review the two pages Comparison of Entities Checklist that you can use to compare the differences between the six major choices in entity selection.

Item	Characteristic	Sole Prop.	Single Member LLC's	"C" Corp.	"S" Corp.	Partnership	LLC
	Title	Owner	Member	Shareholder	Shareholder	Partner	Member
20.	Can specially allocate items of income and expense	N/A	N/A	N/A	No	Yes	Yes
21.	Can deduct interest on money borrowed to <i>invest as business interest</i>	Yes	Yes	No	Yes	Yes	Yes
22.	Can use cash basis even if sales > \$5,000,000	Yes	Yes	No(b)	Yes	Yes	Yes
23.	Inexpensive to form and maintain	Yes	Yes	No	No	No	No
24.	Able to deduct expenses paid personally in computing AGI	Yes	Yes	No	No	Yes	Yes
25.	Can transfer assets 'tax free' where debt > basis	N/A	N/A	No	No	Yes (d)	Yes (d)
26.	Basis for loss includes owner's share of company debt	N/A	N/A	N/A	No	Yes	Yes
27.	Existence of reliable case law	Yes	No	Yes	Yes	Yes	No
28.	Qualifies for ordinary loss under Section 1244	No	No	Yes	Yes	No	No
29.	May offset active income with passive losses	No	No	Yes	No	No	No
30.	Can easily distribute back the owners investment	Yes	Yes	No	Yes	Yes	Yes
31.	Home office deduction	Yes	Yes	No	No	Yes	Yes
32.	Avoid payroll taxes and administration (if no employees except owner)	Yes	Yes	No	No	Yes	Yes
33.	Can deduct medical costs	Yes (e)	Yes (e)	Yes	No	Yes (e)	Yes (e)

Note: A "Yes" answer suggests a favorable response.
Note: A "No" answer suggests an unfavorable response.

- (a) Yes if a limited partner
- (b) Except certain farms and PSC's. See Rev. Proc. 2002-28
- (c) Unimportant with check the box Regs.
- (d) Yes unless partner basis is zero
- (e) Sec. 105/106 health insurance plan

Other considerations:
State Tax Issues
Entities Permitted Multi-state operations
Management Capabilities
Estate Issues
Retirement issues