

Limited Liability Company

By Liliana Parker

A Limited Liability Company, or LLC, is a relatively new business structure allowed by state law. LLC is popular because it's similar to a corporation: owners have limited personal liability for the debts and actions of the LLC, it can be managed by either the members or by managers and has the benefit of pass-through taxation.

All LLCs must be organized with a document called the "articles of organization," specified publicly by the state. LLC ownership can be by one or several natural persons, corporations, partnerships, or other LLCs.

An operating agreement is essential among two or more partners to avoid any future problems. This is a contract among the members that determines, defines, and apportions the rights of the members and the managers.

For federal income tax purposes you have to use IRS Form 1065 but you may elect for the LLC to be taxed as a corporation.

If the only member of the LLC is an individual, the LLC income and expenses are reported on Form 1040, Schedule C, E, or F.

If the only member is a corporation, the LLC income and expenses are reported on the corporation's return, usually Form 1120 or Form 1120S.

LLCs with more than one member file a partnership return, Form 1065.

Employment tax requirements apply to LLCs in much the same way as other types of businesses. Employees are subject to withholding taxes and must file forms W-2 and 1099. For Self-Employment, members are subject to self-employment taxes on earnings and must file Schedule C or F.

Although LLC members' debt liability is limited by the state, they may be held personally liable in situations involving unpaid employee withholdings if they are found to be responsible for making the payments.

Among the LLC's advantages is pass-through taxation. You can elect to be taxed as a sole proprietor, partnership, S corporation or C corporation. Unless the LLC has chosen to be taxed as a corporation, income is retained in the hands of the members as capital gains or as foreign sourced income.

A further advantage is that members are not typically held personally responsible for the debts and liabilities of the business but are still responsible for any debts beyond the fiscal capacity of the entity. Also, a LLC doesn't have ownership restrictions but rather offers flexibility in structuring the management of

the company. It doesn't require as much annual paperwork as a corporation. Written consent of LLC members must be obtained prior to increasing ownership in the company. Lastly, a LLC is perceived as a more professional entity than a sole proprietorship or partnership.

Among the LLCs' disadvantages are that it may be more difficult to raise financial capital for as investors may be more comfortable investing funds in the better-understood corporate structure. As well, some creditors will require members of up-and-starting LLCs to personally guarantee loans, thus making the members personally liable for the debt of the LLC. The management structure may be unfamiliar to many, since doesn't require a board of directors or officers as does a corporation. Lastly, it can be difficult to determine who actually has the authority to enter into a contract on the LLC's behalf, since the principals can use many different titles such as member, manager, managing member, managing director, chief executive officer, president, and partner.