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WHICH FORM OF BUSINESS ORGANIZATION SHOULD I CHOOSE?

A variety of factors will guide your selection of the most appropriate form of business organization. If a business is to be owned and operated by a single individual, the sole proprietorship is a possibility. In most circumstances, however, where multiple persons will be involved as owners of a business enterprise or where capital will be required, the sole proprietorship is not a realistic alternative. The choices, therefore, are ordinarily between the business corporation, the general partnership, and the limited partnership.

THE FOLLOWING FACTORS ARE TYPICALLY RELEVANT IN SELECTING THE APPROPRIATE FORM OF ORGANIZATION:

1. The expense and ease of organizing the business;
2. Whether or not the form of organization results in a distinct legal entity;
3. The expected size and area of operation for the business;
4. Whether or not the form of organization provides continuity of existence for the business beyond the lives of the owners;
5. Whether or not ownership interests in the business may be freely transferrable;
6. The extent to which business owners are entitled to participate in the management and control of the business;
7. The capital and financial needs of the business;
8. The federal income tax treatment of the business and its owners;
9. Whether or not the form of organization provides limited liability for the business owners;
10. The flexibility of organization in being adaptable to special arrangements desired by the participants;
11. The relative ease or difficulty of dissolution in the event of internal dissent or disagreement among the participants.

FOR MOST PEOPLE, THE MOST IMPORTANT FACTORS TO CONSIDER ARE:

- (a) How will I be taxed on the profits of the organization;
- (b) Whether or not my person assets will be protected from liability in the event of an accident;
- (c) Whether or not stakeholder/investors will be entitled to participate in the business' management and control;
- (d) To what extent the business requires outside capital; and,
- (e) The relative ease by which the entity could be dissolved in the event of disagreement.

BUSINESS CORPORATIONS are treated as a separate legal entity and taxpayer for federal income tax purposes. This means that income from the business is taxed to the corporation and any income distributed to the shareholders as dividends is also taxed to them. Limited liability for the shareholders of the corporation is the major advantage of this form of business organization. In some cases, a court may be persuaded to disregard the separate corporate entity and hold the shareholders personally liable, but, ordinarily, the shareholders enjoy limited liability. In an ordinary corporation, the board of directors is elected by the shareholders and granted exclusive authority to manage the affairs of the corporation. This may result in shareholders not participating in the company's management; they may find themselves "locked in" without the voting power to force the company's dissolution. Problems of this sort may be eliminated through the effective drafting of a shareholders' agreement.

GENERAL PARTNERSHIPS are distinguished from a corporation, principally, in that (1) a partnership is

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not recognized as a taxpayer and all items of income, gain, loss and deductions are treated as those of the partners proportionately, (2) all partners are jointly and severally liable for partnership debts and liabilities, (3) there are no restrictions on the partners' freedom to tailor the partnership to fit their particular needs or desires and any partner can always force dissolution of the partnership, although liquidation may be restricted by the terms of the agreement, and (4) each partner is entitled to participate in the management and control of the business on equal terms with other partners, unless the agreement provides otherwise. If a business needs extensive capital investment beyond what the partners themselves have to invest, the general partnership form of organization will usually not be suitable for several reasons.

LIMITED PARTNERSHIPS have historically been an attractive form of organization for a business enterprise, but these characteristics have also involved restrictions and risks that many organizers have found unattractive. The limited partnership is typically created through a voluntary association of persons pursuant to the terms specified in a limited partnership agreement. In some respects a LLC offers many of the attractions of a general partnership and fewer of the problems associated with a corporation, e.g. some of the statutory formalities required of corporations. Unlike the general partnership, however, the limited partnership offers the additional attraction of limited liability for some of the partners, which is not possible in the general partnership. There are, however, certain statutory restrictions on limited partnerships which limit this distinction.

LIMITED LIABILITY CORPORATIONS are a form of business organization recognized by the Internal Revenue Code as a way to reconcile the difference in how corporations and partnerships are treated. In general "members" of a LLC are treated like shareholders or limited partners and "managers" are treated like officers and directors or general partners. Thus, for tax purposes, a LLC may be treated as a partnership while, for state liability purposes, it is recognized as a corporation.

Your choice of business organization should take into consideration the specific circumstances of your planned investment, the nature of each of the owners, what role in management those owners expect to take, and the capital needs of the business. While the steps to register a business entity with the State of Texas are relatively easy, there are several considerations that one should consider when making this decision. Most importantly, each organization should be governed by a document, the bylaws, partnership agreement, or regulations as may be appropriate, that should take into consideration the goals of the owners.

THE ADVICE OF AN ATTORNEY IS IMPORTANT WHEN IT COMES TO CONSIDERING HOW YOUR ENTITY IS TO BE MANAGED.
THE ADVICE OF A CPA IS IMPORTANT WHEN CONSIDERING THE DIFFERENCES IN HOW THESE ENTITIES ARE TAXES.
AS AN ATTORNEY AT LAW AND CPA, WE ARE ABLE TO CONSIDER BOTH ASPECTS OF YOUR INTENDED INVESTMENT.

GIVE US A CALL.

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