

Incorporation (Business Structure & Ownership)

Types of Business Organizations

When organizing a new business, one of the most important decisions to be made is choosing the structure of a business. Factors influencing your decision about your business organization include:

- ✓ Legal restrictions
- ✓ Liabilities assumed
- ✓ Type of business operation
- ✓ Earnings distribution
- ✓ Capital needs
- ✓ Number of employees
- ✓ Tax advantages or disadvantages
- ✓ Length of business operation

The advantages and disadvantages of sole proprietorship, partnership and corporation are listed below.

Sole Proprietorship

This is the easiest and least costly way of starting a business. A sole proprietorship can be formed by finding a location and opening the door for business. It is relatively simple to get started and there is no separate entity to deal with, just the business owner. There are likely to be fees to obtain business name registration, a fictitious name certificate and other necessary licenses. Attorney's fees for starting the business will be less than the other business forms because less preparation of documents is required and the owner has absolute authority over all business decisions.

Sole Proprietorship is not usually recommended if

- ◆ You plan to have employees
- ◆ You are in a business where there is significant risk, or liability involved; or
- ◆ If you want to open your business up to investors.

Partnership

There are several types of partnerships. The two most common types are general and limited partnerships. A general partnership can be formed simply by an oral agreement between two or more persons, but a legal partnership agreement drawn up by an attorney is highly recommended. Legal fees for drawing up a partnership agreement are higher than those for a sole proprietorship, but may be lower than incorporating. A partnership agreement could be helpful in solving any disputes. However, partners are responsible for the other partner's business actions, as well as their own.

Corporation

A business may incorporate without an attorney, but legal advice is highly recommended. The corporate structure is usually the most complex and more costly to organize than the other two business formations. Control depends on stock ownership. Persons with the largest stock ownership, not the total number of shareholders, control the corporation. With control of stock shares or 51 percent of stock, a person or group is able to make policy decisions. Control is exercised through regular board of directors' meetings and annual stockholders' meetings. Records must be kept to document decisions made by the board of directors. Small, closely held corporations can operate more informally, but record-keeping cannot be eliminated entirely. Officers of a corporation can be liable to stockholders for improper actions. Liability is generally limited to stock ownership, except where fraud is involved. You may want to incorporate as a "C" or "S" corporation.

A final word on Forms of Business Ownership

One of the first decisions that you will have to make as a business owner is how the company should be structured. This decision will have long-term implications, so consult with an accountant and or an attorney to help you select the form of ownership that is right for you. In making a choice, you will want to take into account the following:

- Your vision regarding the size and nature of your business.
- The level of control you wish to have.
- The level of "structure" you are willing to deal with.
- The business's vulnerability to lawsuits.
- Tax implications of the different ownership structures.
- Expected profit (or loss) of the business.
- Whether or not you need to re-invest earnings into the business.
 Your need for access to cash out of the business for yourself.