

CORNERSTONE FINANCIAL SOLUTIONS

Individual/Corporate Taxes – Small Business Accounting – Financial Planning

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ENTITY COMPARISON CHART

	SOLE PROPRIETORSHIP	PARTNERSHIP	C CORPORATION	S CORPORATION	LIMITED LIABILITY COMPANY
IRS Pub	334	541	542	None	541
IRS Form	Schedule C, Form 1040	Form 1065	Form 1120	Form 1120S	Form 1065**
Entity Description	A sole proprietorship consists of one individual who carries on an unincorporated trade or business. If a husband and wife carry on a business together as partners, they should file Form 1065, U.S. Return of Partnership Income).	A partnership is an organization having two or more owners that functions as a trade or business. A joint undertaking merely to share expenses or ownership of property does not necessarily constitute a partnership. An LLC with two or more members is generally classified as a partnership for tax purposes.	A corporation is a business entity that carries its own legal status, separate and distinct from its owners. A corporation cannot elect out of corporate taxation.	A corporation can elect to be taxed as an S corporation by filing Form 2553. Only domestic corporations with one class of stock are eligible. An S corporation is limited to 100 shareholders and may not have another corporation as a shareholder.	An LLC is a liability-limiting entity formed under state law. It is treated as a disregarded entity, partnership or corporation for federal income tax.
Taxation	Net profit or loss is computed on Schedule C and is reported as income or loss on the owner's Form 1040.	Partnership income and expenses flow through to the partners. Income is taxed to the partner whether or not distributed.	A C corporation pays tax on its profits. When shareholders take profits from the corporation, the distributions are usually taxable dividends. (Double Taxation)	An S corporation is taxed similar to a partnership. Income and expenses flow through to shareholders.	Same as the disregarded entity, partnership or corporation.
Wages And SE Tax	The owner is subject to SE tax of 15.3% of net earnings from self-employment. SE tax is computed on Schedule SE and is reported as "Other Taxes" on Form 1040. Deduct one-half of SE tax as an adjustment to income on Line 27 of Form 1040.	A general partner's share of business income (including guaranteed payments) is subject to SE tax. A limited partner's share of business income is not subject to SE tax unless the partner performs services for the partnership.	Shareholders who perform services for a corporation, including officers, are treated as employees. Wages of corporate employees are subject to payroll tax and withholding.	An employee-shareholder of an S corporation receives wages for services rendered. These wages must be reasonable. Double taxation of profits is avoided.	Profits are subject to tax in the same way as the disregarded entity, partnership or corporation.
Losses	Business losses can offset other income such as interest, capital gains or a spouse's wages if filing a joint return. Subject to hobby, passive activity and at risk loss rules under Sections 183, 469 and 465, respectively.	Losses flow through to partners. Recognition of loss by a partner is limited by the partner's basis, at-risk rules and passive activity rules. Subject to "hobby loss" rules under Section 183.	Capital losses are allowed only to the extent of capital gains. Net operating loss of a corporation is carried back or forward against corporate income, but is not passed through to shareholders.	Losses flow through to shareholders. Recognition of loss is limited by the shareholder's basis, at-risk rules and passive activity rules. Subject to "hobby loss" rules under Section 183.	Losses are subject to treatment as to the disregarded entity, partnership or corporation.
Fringe Benefits	Amounts paid on behalf of employees are deductible; those paid on behalf of proprietor are not. <i>Exception:</i> Proprietor can deduct medical insurance premiums and reimbursement costs under an accident and health plan that covers all employees. If proprietor's spouse is covered under a plan that also covers owner as part of family, deduction is allowed.	Generally included in partner's income as a guaranteed payment. <i>Exception:</i> Nontaxable benefits include, among others, legal service plans, educational and dependent care programs and certain working condition and <i>de minimis</i> fringe benefits and employee achievement awards.	Owner-employees are entitled to the same tax-free fringe benefits as other employees (subject to discrimination rules).	Generally included in income for employee-shareholders owning more than 2% of stock. <i>Exceptions:</i> contributions to retirement plans, compensation for injury or sickness, educational and dependent care programs, employee discounts, working condition and <i>de minimis</i> fringes and no-additional-cost services.	Same as the disregarded entity, partnership or corporation.
Personal Liability	The sole proprietor is liable for all business debts and actions.	General partner personally liable for all partnership debt. Limited partner's liability usually limited to investment in partnership.	Shareholders not liable for debts incurred by corporation. Liability generally limited to amount invested. *	Shareholders not liable for debts incurred by corporation. Liability generally limited to amount invested. *	The degree of liability protection for LLC members varies from state to state.

* **Caution:** The courts may disregard the so-called "corporate liability shield" in the case of single shareholder corporations.

** A disregarded single-member LLC is included in the tax form of its owner (1040, 1120, etc)