Corporation

A corporation (sometimes referred to as a C corporation) is an independent legal entity owned by shareholders. This means that the corporation itself, not the shareholders that own it, is held legally liable for the actions and debts the business incurs.

Corporations are more complex than other business structures because they tend to have costly administrative fees and complex tax and legal requirements. Because of these issues, corporations are generally suggested for established, larger companies with multiple employees.

For businesses in that position, corporations offer the ability to sell ownership shares in the business through stock offerings.

Corporation Taxes

Corporations are required to pay federal, state, and in some cases, local taxes.

Unlike sole proprietors and partnerships, corporations pay income tax on their profits. In some cases, corporations are taxed twice - first, when the company makes a profit, and again when dividends are paid to shareholders on their personal tax returns.

Structure

A corporation has shareholders, directors and officers. Shareholders are the owners of the company and elect the board of directors, who in turn oversee and direct corporation affairs and decision-making but are not responsible for day-to-day operations. The directors elect the officers to manage daily business affairs.

Limited liability protection.

A corporation offers limited liability protection, so shareholders (owners) are typically not personally responsible for business debts and liabilities.

Advantages of a Corporation

- **Limited Liability.** When it comes to taking responsibility for business debts and actions of a corporation, shareholders' personal assets are protected. Shareholders can generally only be held accountable for their investment in stock of the company.
- **Ability to Generate Capital.** Corporations have an advantage when it comes to raising capital for their business - the ability to raise funds through the sale of stock.
- **Corporate Tax Treatment.** Corporations file taxes separately from their owners. Owners of a corporation only pay taxes on corporate profits paid to them in the form of salaries, bonuses, and dividends, while any additional profits are awarded a corporate tax rate, which is usually lower than a personal income tax rate.
- **Attractive to Potential Employees.** Corporations are generally able to attract and hire high-quality and motivated employees because they offer competitive benefits and the potential for partial ownership through stock options.

Disadvantages of a Corporation

- **Time and Money.** Corporations are costly and time-consuming ventures to start and operate. Incorporating requires start-up, operating and tax costs that most other structures do not require.
- **Double Taxing.** In some cases, corporations are taxed twice - first, when the company makes a profit, and again when dividends are paid to shareholders.
- **Additional Paperwork.** Because corporations are highly regulated by federal, state, and in some cases local agencies, there are increased paperwork and recordkeeping burdens associated with this entity.

S corporation vs. C corporation:

Taxation.

Taxation is often considered the most significant difference for small business owners when evaluating S corporations vs. C corporations.

C corporations.

C corps are separately taxable entities. They file a corporate tax return (Form 1120) and pay taxes at the corporate level. They also face the possibility of double taxation if corporate income is distributed to business owners as dividends, which are considered personal income. Tax on corporate income is paid first at the corporate level and again at the individual level on dividends.

S corporations.

S corps are pass-through tax entities. They file an informational federal return (Form 1120S), but no income tax is paid at the corporate level. The profits/losses of the business are instead “passed-through” the business and reported on the owners’ personal tax returns. Any tax due is paid at the individual level by the owners.

Personal Income Taxes.

With both types of corporations, personal income tax is due both on any salary drawn from the corporation and from any dividends received from the corporation.

Corporate ownership.

C corporations have no restrictions on ownership, but S corporations do. **S corps are restricted to no more than 100 shareholders**, and shareholders must be US citizens/residents. S corporations cannot be owned by C corporations, other S corporations, LLCs, partnerships or many trusts. Also, S corporations can have only one class of stock (disregarding voting rights), while C corporations can have multiple classes. C corporations therefore provide a little more flexibility when starting a business if you plan to grow, expand the ownership or sell your corporation.