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Similarities Between a Partnership & a Limited Company

By: Neil Kokemuller
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Partnerships and limited liability companies present several similarities for business owners looking for the right company structure. Both have similar income distribution and tax-reporting formats, and both are simpler to set up and operate than a corporation.

Limited Liability

All owners may have unlimited personal liability with a partnership, but establishing a business as a limited partnership leaves most owners insulated from such risks. Within a limited partnership structure, only one general partner assumes unlimited liability. All inactive, limited partners have limited liability, just as they do with an LLC.

Tips

Income Distribution and Tax Reporting

LLCs. In both setups, profit normally is shared evenly among the owners unless agreed upon differently in writing. For certain partnerships, partners may agree to invest different amounts of resources, and therefore profit unequally.

Income is treated as pass-through for both business types in tax reporting as well. Pass-through income means the company isn't taxed on profits before they are distributed to owners. In a corporation, the business pays taxes and then the remaining income is shared with owners, who then pay taxes. Avoiding the double-taxation allows owners to pocket more of the company's income.

Simpler Structures

LLCs are a bit more complex to form than a general partnership, but both are less complicated than setting up a corporation, according to the legal website Nolo. General partnerships are sometimes as simple as pooling resources, getting a building when necessary, and actively engaging in business operations. Some states require more formal paperwork for certain types of partnerships. LLCs require formal registration within the state of operation, but the documentation and time involved are still modest compared to the articles of incorporation and other requirements to form a corporation.

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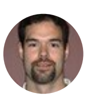

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An S Corporation is one of several optimal structures for a small business. It blends some of the benefits of a sole proprietorship with those of a C Corporation. An S Corporation is often considered alongside a limited liability company when someone is looking for something more formal than a sole proprietorship.

Single Taxation

Like an LLC, an S Corporation has pass-through taxation, which means you only pay taxes once. The profits of the business are distributed to owners, who then pay taxes on their share of the earnings. In contrast, a C Corporation experiences double-taxation. The business pays taxes on corporate earnings and each shareholder pays taxes on his share of the distributed earnings. By working for the business and receiving a salary, an S Corporation owner also may avoid hefty self-employment penalties common with a sole proprietorship.

Simplicity and Asset Protection

An S Corporation is easy to set up relative to other formal business structures. Some people operate as sole proprietors just to avoid formalizing their operation. However, an S Corporation allows for greater credibility with customers, partners and suppliers. Similar to a C Corporation or LLC, an S Corporation also insulates the personal assets of owners, because the business is treated as a separate legal entity from its owners. If the company is sued, for instance, the business assets are at risk, but not the financial assets of owners.

Ownership Restrictions

An S Corporation does have a few more setup and ownership restrictions than an LLC. First, you must be a U.S. citizen or legal resident to form an S Corporation. Also, whereas C Corporations and LLC allow unlimited ownership, an S Corporation is limited to 100 shareholders. Profit distribution or dividends must align with a shareholder's level of ownership. If someone owns 5 percent of the business, he must receive 5 percent of income distributions. LLCs have more distribution flexibility.

Setup Costs

There are more costs to setting up an S Corporation than there are with an LLC. As with C Corporations, you file formal legal documents and pay related fees to set up an S Corporation. Annual report filing fees and franchise fees are additional costs that you may pay with an S Corporation that you don't incur with a partnership or sole proprietorship.

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