Title:
Subchapter S Corporation Tax Status

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Summary:
Overview of the Subchapter S Corporation Designation

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Article Body:
Overview of the Subchapter S Corporation Designation

Although the term Subchapter S Corporation sounds as if it applies to a certain type of company, in actuality, it is merely a term used by the IRS (Internal Revenue Service) to designate a particular tax status. Almost any company that is comprised of 75 or less shareholders can apply for the Subchapter S Corporation tax status designation. Being approved for a Subchapter S Corporation status allows the company to be taxed as if it were a partnership or sole proprietorship. An application is generally submitted just after a company has incorporated. At any time a company may choose to withdraw from Subchapter S Corporation tax status by filing another form with the IRS. Withdrawals must be submitted prior to the beginning of a new tax year.

Subchapter S Corporation Eligibility Requirements

In order for a business to qualify as an S Corporation, there are several eligibility requirements that need to be met. Any corporation that meets the following criteria can be approved for Subchapter S Corporation status:

* The company must have 75 or fewer shareholders, and each shareholder must agree to file as an S Corporation.

* Every stockholder must be a resident and citizen of the United States
* Stock sold by the company must be of a single class
* The company is required to use the calendar year as the official fiscal year

If a corporation meets these requirements, they must file form 2553 with the IRS to be granted Subchapter S Corporation tax status.

Advantages to Subchapter S Corporation Status

This tax status is appealing to many business owners for several reasons. The primary advantage to filing as an S Corporation is that income is passed through directly to the shareholders who file corporate income with their personal taxes. In this manner, the corporation avoids being taxed twice for the same income. In most cases, S Corporations do not pay any income tax and losses are absorbed by the shareholders instead of the corporation. Additional advantages to Subchapter S Corporation tax status includes:

* Return on investment earnings do not fall under self-employment tax status providing the shareholder/employee receives reasonable compensation for their work.

* Financial documentation and accounting is less complicated than that required by traditional corporations.

* S Corporation status may provide easier access to credit resources, depending on the business history of the corporation.

Disadvantages to Subchapter S Corporation Status

When considering whether or not to file for Subchapter S Corporation tax status, companies should also be aware of potential disadvantages. Because the financial power is in the hands of the shareholders, executive decisions need to be agreed upon by all. Disagreements between individual shareholders can lead to a stall in the process. Additionally, stockholder/employees must declare health insurance and other employee benefits as taxable income if they own more than a 2% share of stock. Subchapter S Corporation tax status is most beneficial to corporations with small numbers of shareholders that have a common vision for the future of the company.