

# DCCA's Guide to Choosing the Right Legal Form For Your Business

Source: [www.hawaii.gov/dcca](http://www.hawaii.gov/dcca) Jan. 2013

Issues to Consider	Sole Proprietorship	Partnership	Corporation	Sub S Corporation	Limited Liability Partnership	Limited Liability Company
<b>Ownership</b>	By a single individual	By two or more persons	By unlimited number of shareholders	By shareholders: number of shareholders limited to 100, no foreign investors	2 or more persons or entities	1 or more persons or entities
<b>Business Registration (State Dept. of Commerce &amp; Consumer Affairs)</b>	Not required, unless public notice of trade name is desired	Within 30 days after formation, file Certificate of Limited Partnership or General Partnership forms.	File Articles of Incorporation. For non-Hawaii corporations, file Application for Certificate of Authority with a Certificate of Good Standing	Same as C corporation "S election" is made with the federal Internal Revenue Service on Form 2553	File a General Partnership form with a Statement of Qualification. For non-Hawaii LLPs, file as a Foreign LLP.	File Articles of Organization. For non-Hawaii LLCs, file a Certificate of Authority for LLCs
<b>Management (Control)</b>	Entirely in hands of owner	By general partners	Corporation's board of directors	Same as corporation	By general partners	Member-managed or manager-managed
<b>Life of the Business</b>	Will terminate with death or disability of owner	Generally for a specific, agreed-upon term. May be terminated by death, withdrawal, insolvency or legal disability of a general partner	Perpetual, unless by state law or charter	Same as corporation	Same as general partnership	May be for a specific agreed-upon term or at will
<b>Liability</b>	Owner liability unlimited. Personal property can be attached by creditors to settle business debts	Unlimited for general partners. General partners are jointly and severally liable for obligations of partnership. In LP, Limited Partner's liability limited to amount invested	Shareholders' liability limited to their investment in corporate stock	Same as corporation	Limited to amount of investment	Limited to amount of investment or as specified in Articles of Organization
<b>Taxation</b>	Owner taxed on business profits on Form 1040. Business does not file a separate tax return. Subject to self-employment tax (SE Tax)	Income passed-through to partners for income tax purposes. Business files information return Form 1065. Partners file on 1040, subject to SE Tax	Corporation taxed on taxable income on Form 1120, whether or not distributed to shareholders. Shareholders taxed on dividends distributed by corporation	Shareholders taxed on some taxable income of the corporation, whether or not distributed; subj to SE Tax. Entity must also report and pay taxes on Form 1120S certain types of income.	Same as general partnership	Members taxed on share of company income using Forms 1040 and/or 1065. Or, can elect to be treated as a corporation for tax purposes using Form 1120 or 1120S (select on Form 8832)
<b>Advantages</b>	<ul style="list-style-type: none"> <li>*Simplicity</li> <li>*Ease of formation</li> <li>*Greater flexibility of action</li> <li>*Singleness of control</li> <li>*Maximum centralized authority</li> </ul>	<ul style="list-style-type: none"> <li>*Very flexible in working out complex deals</li> <li>*Ease of formation</li> <li>*Increased sources of capital</li> <li>*Increased source of managerial skills</li> </ul>	<ul style="list-style-type: none"> <li>*Legal entity separate from individuals</li> <li>*Limited personal liability</li> <li>*Continuity of existence</li> <li>*Continuity of management</li> <li>*Easier to raise capital</li> <li>*Readily transferable and variable interests</li> <li>*Adaptable to small and large businesses</li> </ul>	<ul style="list-style-type: none"> <li>*Legal entity separate from individuals</li> <li>*Limited personal liability</li> <li>*Continuity of existence</li> <li>*Continuity of management</li> <li>*Readily transferable interests</li> <li>*Slight advantage in SE Tax (wages vs. distributions)</li> </ul>	<ul style="list-style-type: none"> <li>*Division of responsibilities</li> <li>*Ease of formation</li> <li>*Limited personal liability</li> <li>*Greater flexibility of action</li> <li>*Increased sources of capital</li> </ul>	<ul style="list-style-type: none"> <li>*Legal entity separate from individuals</li> <li>*Limited personal liability</li> <li>*Ability to customize lifespan, managerial control, taxation</li> <li>*No corporate formalities to follow</li> <li>*Possible to raise capital readily</li> <li>*Possible to have readily transferable interests</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>*Unlimited personal liability</li> <li>*Legal life ends with owner's death</li> <li>*Difficult to raise capital</li> <li>*Possible personnel difficulties</li> <li>*Owner's salary cannot be treated as an expense, hence, not tax deductible</li> </ul>	<ul style="list-style-type: none"> <li>*Unlimited personal liability</li> <li>*Impermanence of existence</li> <li>*Division of control/authority</li> <li>*Difficult to find compatible partners</li> <li>*Difficult to raise additional capital</li> <li>*Owners' salary/wage cannot be treated as an expense, hence, not tax deductible</li> </ul>	<ul style="list-style-type: none"> <li>*Difficult, costly formation, must observe formalities</li> <li>*Subject to close government regulation</li> <li>*Scope limited by corporate charter</li> <li>*Inflexibility of operations</li> <li>*Double taxation by paying both corporate and personal income taxes</li> </ul>	<ul style="list-style-type: none"> <li>*Only one class of stock outstanding (less flexible than C corporations)</li> <li>*Same as other disadvantages listed for C corporations</li> </ul>	<ul style="list-style-type: none"> <li>*Impermanence of existence</li> <li>*Division of control/authority</li> <li>*Difficult to find compatible partners</li> <li>*Difficult to raise additional capital</li> <li>*Owners' salary/wage cannot be treated as an expense, hence, not tax deductible</li> </ul>	<ul style="list-style-type: none"> <li>*Difficult, costly formation because of flexibility and many options</li> <li>*Scope limited by company charter</li> </ul>

