



---

## Small Business Builder: Becoming Limited Liability Company

### Becoming a Limited Liability Company

**Third in a series**

**By Mary Campbell**

**March 14**

It's easy in the state of Anarchy.

Pratt Falls and Hi Jinx are general partners in the company FJ Entertainment. Pratt founded the company as a sole proprietorship to provide children's entertainment. Finding that he was more amusing when working with Hi than he was on his own, he took Hi on as a partner.

Now they want to add pony rides and hire employees. To do so, they need to raise capital. There are also greater risks (for example, they could be sued if a child falls off a pony or if an employee is injured on the job). And, after all, one of the partners is named "Jinx." Pratt (more business-savvy than Hi) considers incorporating, which would, to some extent, protect personal assets from liability for lawsuits and company indebtedness. They could get the protection with liability insurance, but they also want to raise money by selling shares.

In the end, however, Pratt chooses a fairly new form of organization □ the limited liability company, or LLC.

Here's Why, More or Less

**Fewer dollars:** FJ Entertainment is located in the state of Anarchy (east of Virginia and south of Louisiana). Though the company must file with the state (just as for a corporation), in Anarchy, as in most states, it is less expensive and complicated to set up an LLC than it is to set up a corporation.

**Fewer hassles:** LLCs need not conduct annual meetings, prepare annual reports or follow many other rules that apply to corporations (though Pratt happens to think that having annual meetings and reports is a good idea).

**More protection:** The LLC shields its owners' personal assets in the same way a corporation does.

**More members, more money:** An LLC is owned by "members." To raise money to buy, house and care for ponies, the company can sell interests to members □ as many or as few as needed.

**More flexibility:** There is great latitude in operating an LLC. The members can elect managers just as a corporation elects directors, or they can run the company themselves.

The Beauty □s in the Flexibility

The same flexibility applies to taxation. The LLC can choose to be taxed as a corporation (an advantage if it wants to retain earnings, which would be taxed at the lower corporate rate) or as a partnership (permitting "pass-through" taxation and thus avoiding the double-tax dilemma, although the

latter choice limits the tax-free fringe benefits available to corporate owners).

In fact, the beauty of an LLC is its flexibility. The members can organize the company, and allocate profits and losses, almost any way they can agree on. S corporations, on the other hand, may have no more than 75 owner-shareholders (who must be U.S. residents and individuals, not companies) and cannot own 80 percent or more of another company's shares. There are no such restrictions on LLC members (companies and nonresident aliens are allowed) or on LLC subsidiaries.

S corporation stock may be freely transferred □ not the case with an LLC, which also has a finite lifespan □ while corporations are considered "perpetual."

Pratt Falls finds neither of these restrictions troubling, and in any case he has missed the March 15 deadline to file for election of S corporation status.

Here's How, Basically

Pratt's lawyer offers to "take care of everything," from filing for LLC status to reserving the company's name to handling "all the other details" □ for the usual \$150 per hour plus expenses.

A host of online vendors offer to "take care of everything" for a minimum of \$75 plus this and that. Pratt makes a phone call to the state corporation commission and finds that in Anarchy it costs \$50 to file the LLC's articles of organization □ more if the company wants to operate in a foreign country, but Pratt doesn't foresee taking the ponies to Argentina any time soon.

Naturally, he goes the do-it-yourself route, opting to spend an extra \$35 for "expedited service," although Pratt likes to think of it as the pony express.

An editor since the age of 6, when she returned a love letter with corrections marked in red, Mary Campbell founded Zero Gravity in 1984 to provide writing, editing and marketing services. Small Business Builder is published on Wednesdays.

Copyright © 2007 ABC News Internet Ventures