LLC vs. Inc. Which Is Better for Your Business?

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New business owners often get conflicting advice about whether to set up a **limited liability company** or a corporation.

Both are formed by filing paperwork with the state, and both help to protect owners from liability if the business is sued or runs into financial trouble. There are, however, differences in the way LLCs and corporations are managed and taxed.

Inc. vs. LLC: Liability Protection

The owners of both LLCs and corporations are protected from personal liability for business debts or lawsuits. This means that if the business is sued or faces collection action from creditors, your personal assets—such as your house, your car, and your personal bank accounts—are safe. You may, however, lose the money that you have invested in the business.

Which is better? As a business owner, you will receive the same type of liability protection regardless of whether you form an**LLC or corporation**.

LLC vs. Corporation: Management and Profit-Sharing

Corporations have a standard and predictable management structure. Every corporation must have a board of directors that oversees the “big picture," officers who run the business day to day, and shareholders who own stock in the company. Shareholders meet annually, and they receive company profits based on the number and type of shares they own. It's relatively easy to add new shareholders to a corporation, or to transfer shares from one person to another.

LLCs don't have to use any particular management structure. They can be managed by their owners (who are known as “members") or by a group of managers. There are no required job titles, and a small member-managed LLC might be run rather informally. Each member owns a certain percentage interest in the LLC, but profits can be distributed in any way that the members agree to. However, LLC membership isn't as easily transferred as corporate stock.

Which is better? It depends. Because corporations have a uniform management system and easy transferability of shares, investors tend to prefer corporations over LLCs. Small businesses that aren't looking to raise outside capital often like the flexibility and relative informality of an LLC. Neither type of business has limits on the number of owners it can have.

Corporation vs. LLC: Taxes

Corporations can be taxed in one of two ways:

- Any corporation can be taxed as a **C corporation**. A C corporation pays **corporation taxes** on its profits. If shareholders receive dividends, they pay personal income tax on them. This double taxation of dividends is often cited as a disadvantage of C corporations.
- Some corporations can choose **S corporation** taxation instead. An S corp. doesn't pay corporate income tax. Instead, all of its profits pass through to the shareholders, who pay personal income tax on them. This "pass through" taxation often saves money, but not all corporations can take advantage of it. For example, corporations that have more than 100 shareholders, more than one class of stock, or foreign shareholders cannot choose S corporation taxation.

LLCs do not have their own tax classification. Usually, single-member LLCS pay **LLC taxes** as though they were sole proprietorships, and multi-member LLCs are taxed as though they were partnerships. The LLC's income and expenses are reported on the members' personal income tax returns, and each member pays tax on his or her share of the profits. However, an LLC can also choose to be taxed as either an S corporation (if it qualifies) or a C corporation.

What does this mean in practical terms? Here are some things to consider:

- Outside investors may prefer that a business be a C corporation.
- S corporations offer tax savings for many small businesses, but a C corporation can be a good choice for a business that plans to keep cash in the company instead of distributing it to owners.
- LLCs offer pass-through taxation without the ownership restrictions that are imposed on S corporations. A business that can't be an S corporation might still have pass-through taxation if it is set up as an LLC.
- If the owners work in the business, they may save on self-employment taxes by setting up an S corporation instead of an LLC.

Business taxes can be complex. Before you **incorporate a business** or **start an LLC**, it's wise to consult with a tax professional to find out which tax status is best for your particular situation.

LLC or Inc.: Recordkeeping Requirements

Corporations must have an annual shareholders' meeting, and most states require corporations to keep minutes of their meetings and records of important resolutions. This is true even if the corporation has only one or two owners. Corporations also must keep shareholder records, and in many states they must file an annual report and pay an annual fee to the state.

LLCs also should keep good records, but in most states the actual requirements are more minimal than the requirements placed on corporations. LLCs do not have to hold annual meetings, and they are less likely to have an annual report requirement. This is appealing to small business owners who don't want the hassle of additional paperwork.

So, **LLC vs. Inc.**, which is better for your business? Although corporations and LLCs offer the same liability protection, there is a **difference between LLC and Inc**. The one you choose for your business will depend on the number of owners you have, your plans for expansion or outside investment, the way you plan to run the company, and the tax consequences of each choice.