

## PROFESSIONAL ENGLISH by M. Belogash

### UNIT 13 BUSINESS LEGAL STRUCTURE

#### 13.1 Getting started.

Now that you have decided to start your own business, you will have to determine what business structure or form of organization suits your needs. The structure of your business will depend on whether you want to run your business yourself or with a partner or associates. There are three basic types of business structures and a lot of hybrids to meet different entrepreneurial needs and ambitions.

#### Discuss the following points:

1. What do you think are the main considerations of a businessman or a group of businessmen when starting a firm?

#### 13.2 Look through the following vocabulary notes which will help you understand the text and discuss the topic.

sole proprietorship (Am. E.); sole trader (Br. E.)	индивидуальное частное предприятие, единоличное владение, индивидуальное предпринимательство
general partnership	командитное товарищество, товарищество на вере, полное товарищество, компания с неограниченной ответственностью
limited liability partnership	товарищество с ограниченной ответственностью
corporation	отдельная фирма, корпорация, акционерное общество
S corporation	корпорация, соответствующая подразделу S «Кодекса о внутренних доходах США»
IRS (Internal Revenue Service)	Служба по внутреннему налогообложению США

Internal Revenue Code	«Кодекса о внутренних доходах США»
C corporation	корпорация, соответствующая подразделу С «Кодекса о внутренних доходах США»
professional associations	профессиональное объединение
limited liability company (LLC)	акционерная компания/общество с ограниченной ответственностью (ООО)
business trusts	деловой траст (форма неакционерного предприятия с ограниченной ответственностью), деловой доверительный паевой фонд, коммерческий траст
professional corporations	профессиональная корпорация
liability	имущественная ответственность, обязательство
limited liability	ограниченная ответственность
unlimited liability	неограниченная ответственность
continuity of existence	непрерывность деятельности предприятия
transferability	передаваемость, перемещаемость, обращаемость, возможность передачи другому лицу
formality	соблюдение формальностей, специальная процедура
a tort	гражданское правонарушение
tort risk	риск гражданских правонарушений
contract risk	контрактный риск
(un)intentional	(не) преднамеренный
working injury	производственная травма
product liability	ответственность производителя, ответственность за качество выпускаемой продукции
vendors	поставщик услуг; оптовая фирма, предлагающая товар
customers	покупатели
a tradeoff	компромисс

pass-through taxation	сквозное налогообложение, принцип налогообложения, когда прибыль, полученная компанией, не облагается налогом на уровне самой компании, а рассматривается как доход, полученный напрямую ее учредителями
(un)intentional	(не)преднамеренный
a tradeoff	компромисс, соотношение
to file a tax return	подать налоговую декларацию о доходах
personal tax return	поступления от личного подоходного налога
asset purchase agreement	договор о приобретении активов
interest transfer	имущественное право, доля, пакет акций, процентный доход
estate	имущество, собственность
to transfer	передавать
tax-reporting	налоговая отчетность
tax-paying	налоговые выплаты
latitude	свобода, широта, терпимость
best tax rates	самые низкие налоговые ставки
to be sued	отвечать по иску в суде
voting rights	право голоса
general partner	полный товарищ/партнер
limited partner	участник-вкладчик или коммандитист
a separate entity	самостоятельное образование/субъект
right of first refusal	право первого выбора, право преимущественной покупки
a venture	предприятие
to incorporate	регистрировать в качестве юридического лица, инкорпорировать
name check	идентификация имени
an incorporator	учредитель; лицо, подающее документы на регистрацию

Articles of Incorporation (Am.E.); Memorandum of Association (Br. E.)	свидетельство о регистрации корпорации/компании; устав корпорации
registered office, syn. legal office (здесь)	юридический адрес, официальный адрес правления корпорации
registered agent	регистрационный агент, специальное лицо, указываемое в учредительных документах
business office	служебное помещение
to file	подавать, регистрировать документ
board of directors	совет директоров
to sit on the Board	быть членом совета директоров
level of leverage	уровень заемного капитала
leverage (Am. E.); gearing (Br. E.)	экономический рычаг; соотношение собственного и заемного капитала
domestic corporation	отечественная корпорация
state statute	закон штата
members	участники
grantors	лица, передающие право
declaration of trust	декларация об учреждении траста, юридический документ о принятии доверительным управляющим права на имущество в интересах учредителя или иного бенефициара
unanimity	единогласие
a private limited company (LTD) (Br. E.)	частная компания закрытого типа
a public limited company (PLC) (Br. E.)	частная компания открытого типа
a public corporation (Br. E.)	государственная корпорация (Брит.)

### 13.3 Reading

#### Forms of Business Organization in the USA

There exist a number of different business structures that differ in several important aspects. Some of the most common business structures are:

- sole proprietorship

- general partnership
- limited partnership
- limited liability partnership
- corporation (including S corporations)
- professional associations
- limited liability companies
- business trusts
- professional corporations

There are six common issues that distinguish the different business forms: taxation, liability, risk and control, continuity of existence, transferability, expense and formality. Taxation and risk and control are the more significant issues. In addition to these common issues, there are also issues specific to each of them.

A one-person firm generally has only three choices of business form: sole proprietor, corporation or a limited liability company. Multiple people typically have the additional options of general partnership, limited partnership, or a limited liability company.

Liability is a risk that one exposes oneself to when starting a business. Two types of risk are tort risk and contract risk. A tort is unintentional or intentional harm to a person or a property of another. Some examples of tort risk are working injury, product liability and general liability such as when somebody falls on a wet floor. Examples of contract risk are financing risk and risk with vendors and customers. Tort risk can be protected against by using insurance. Most businesses can get an insurance policy against all tort risks. Liabilities associated with the contract can be limited in the contract itself.

Traditionally there was a tradeoff between liability and taxation. However, S corporations and LLCs have changed that tradeoff so that a company can have limited liability and pass-through taxation.

**Sole proprietorship** As the simplest form of business legal structure the sole proprietorship is viewed as being one and the same as its owner. This characteristic has the advantage of simplicity but also has a disadvantage of personal liability. A sole proprietorship has pass-through taxation; the business itself does not file a tax return; the

income is reported on the personal tax return. The owner of a sole proprietorship has unlimited personal liability. However, with insurance of tort risk and contractual limitations for contract risk, the sole proprietor can insure against most risks and operate with nearly the same level of comfort as the owners of the corporation. A sole proprietorship exists only as long as the owner is alive or until the owner decides to close the business. The control belongs entirely to the owner, who also assumes the full risk of the business. Transferring one's interest in a sole proprietorship is very easy – one simply prepares an asset purchase agreement and sells the assets. The assets of a sole proprietorship are transferred with the estate of the owner upon death. It is the simplest way of doing business. The costs of formation are very low and there is little formality required.

**General partnership** The general partnership (or simply partnership) is an association of two or more people carrying on a business with the goal of earning profit. A partnership is viewed as being the same as its owners. There is little formality involved in creating a partnership. Like a sole proprietorship, a partnership has only one level of taxation. A partnership is a tax-reporting, not a tax-paying entity. There is latitude in allocating income according to which partners have the best tax rates.

While pass-through taxation is an advantage, owners of a partnership have an unlimited personal liability. Generally, each partner in a partnership is jointly liable for the partnership's obligations. Joint liability means that partners can be sued as a group. Three rules for liability in a partnership are: 1. Every partner is liable for his or her own actions. 2. Every partner is liable for the actions of the other partners. 3. Every partner is liable for the actions of the employees of the business. Partners are given equal voting rights, even if they contributed different amounts of capital.

**Limited partnership (LP)** A limited partnership consists of two or more persons, with at least one general partner and one limited partner. While a general partner has unlimited personal liability, a limited partner's liability is limited to the amount of his or her capital

invested in the firm. The limited partnership is a separate entity and must file taxes as a separate entity. LPs are especially useful for raising capital since they permit investors to participate financially in a business without incurring personal liability. A limited partnership normally has pass-through taxation, but must meet certain criteria to avoid being taxed as a corporation. The limited partner interest is considered a security by law. It can be transferred to a third party, but general partners and limited partners have the right of first refusal.

**Limited liability partnership (LLP)** A limited liability partnership is similar to a limited partnership except that all partners in an LLP enjoy limited liability. LLPs are common among professionals such as attorneys and accountants, who are not allowed to use corporations to limit their liability. LLPs offer both the pass-through taxation of a partnership and the liability protection of a corporation.

**Corporation** The corporation is the most common form of business entity among larger firms. Unlike sole proprietorships and partnerships, corporations are separate and distinct from their owners in the eyes of the law. The owners' liability is limited to the amount of capital invested in the corporation. It is a legal entity which has the rights and duties of an individual: it can be sued, taxed, taken to court, etc.

The corporate business form was well-developed under Roman law. In the second and third centuries the corporate form was used by the early Christian church to hold and transfer church property. The corporate form was brought to the American colonies by the British.

A venture does not need to incorporate in its very early stages. The need for incorporation usually arises from a specific event such as a need for external financing or selling a product opening up potential liability, etc. To form a corporation, an incorporator performs a name check. The incorporator then files the articles of incorporation which include: the name, the address of the corporation's registered office and the name of the registered agent in the office (the legal office is not the same as the corporation's business office), the length of time that the corporation is to exist, the capital structure (common stock

and preferred stock), the name and the address of the incorporator. Up to this point in the incorporation process, one has spent no more than a few hundred dollars in fees for filing the articles of incorporation. The incorporator then elects the board of directors and goes away as the board of directors takes over. The directors then issue shares and elect the officers.

**C corporation** For a corporation organized under subchapter C of the 1986 IRS code (known as C corporation), the federal tax ranges from a minimum of 15% to a maximum of 35%, depending on the corporation's level of taxable income. Double taxation may be the issue with C corporations since profits paid out as dividends are taxed a second time at the personal level. To reduce the tax burden the corporation can include debt in its capital structure, but at a certain level of leverage the IRS will reclassify the debt as equity. A more common way of reducing the tax burden is to pay year-end bonuses so that the corporate income is reduced to near zero. However, there is a limit to what the IRS considers reasonable compensation.

**S corporation** For a corporation organized under subchapter S of the Internal Revenue Code (S stands for small business corporation) there is a pass-through taxation. The S corporation must be a domestic corporation with the maximum number of shareholders of 75 which include individuals or certain estates and trusts who are not non-resident aliens. Besides, S corporations must have one class of stock.

**Limited liability company (LLC)** A Limited Liability Company is a business structure allowed by state statute. LLCs are popular because, similar to a corporation, owners have limited personal liability for the debts and actions of the LLC. Other features of LLCs are more like a partnership, providing management flexibility and the benefit of pass-through taxation. Owners of an LLC are called members. Since most states do not restrict ownership, members may include individuals, corporations, other LLCs and foreign entities. There is no maximum number of members. Most states also permit "single member" LLCs, those having only one owner.

**Business trusts** These trusts are unincorporated and are typically created as alternatives to corporations or partnerships. The business trust can conduct a wide variety of business, including



investing, buying, and selling, yet offers beneficiaries a limited level of liability; a business trust may even invest in stocks, bonds, and similar investment instruments. Unlike corporations, business trusts do not receive charters from the states in which they are formed. Instead, they are formed through the creation of declarations of trust, which their grantors voluntarily sign.

**Professional corporation** A professional corporation is a variation of the corporate form of business organization that is available to entrepreneurs who provide professional services—such as doctors, lawyers, accountants, consultants, and architects. "Professionals," Frederick W. Dailey explained in his book *Tax Savvy for Small Business*, "are treated as small businesses under the tax code. Most of them operate as sole proprietorships or partnerships, and are subject to the same tax rules as other similar businesses. However, certain professionals who offer services may form and operate a special type of entity, called a professional corporation." Some states require professionals to form this type of entity if they wish to incorporate. In a professional corporation, the owners perform services for the business as employees.

## **13.4 Comprehension**

### **13.4.1 Answer the questions using the active vocabulary and Unit 13 Glossary.**

1. What are the six common issues that distinguish the different business forms?
2. Why do you think taxation and risk and control are the more significant issues?
3. What are the choices of business form for a one-owner firm?
4. What are the choices of business form for multiple people?
5. What are the two types of risk that one exposes oneself to when starting a business?
6. What is the tradeoff between liability and taxation?
7. How have S corporations and LLCs changed that tradeoff?
8. What are the major characteristics of a sole proprietorship?
9. What are the major characteristics of a partnership?
10. What are the major characteristics of a corporation?
11. What types of partnership do you know?

12. What types of corporation do you know?
13. What are the advantages of a limited liability company over other legal types?
14. What is the major difference between a business trust and a corporation?
15. What is the variation of the corporate form of business organization that is available to entrepreneurs who provide professional services?

**13.4.2 Complete the following chart. Make use of Glossary 13 and the text 13.3.**

	Taxation	Liability	Risk and control	Continuity of existence	Transfer ability	Expense and formality
sole proprietorship						
general partnership						
LP						
LLP						
S corporation						
C corporation						
LLC						
business trust						
professional corporation						

**13.4.3 Mark these statements T(true) or F(false) according to the information in the Text and Unit 13 Glossary. If they are false say why.**

1. The term ‘company’ is typical for US forms of business organization.

2. The term 'corporation' is typical for UK forms of business organization.
3. The term 'company' is not used to refer to any US form of business organization.
4. Multiple people can typically have the limited liability options of business form.
5. The term 'corporation' is not used to refer to any UK form of business organization.
6. The two basic liability alternatives are unlimited liability, which has no restrictions on ownership liability, and limited liability, which does have restrictions.
7. In a business partnership, the parties that join forces could be individuals, corporations, trusts, other partnerships, or a combination of all of the above.
8. The advantages of a corporation are that it is easy to establish, can draw upon the financial and managerial strength of all the owners, and the profits are not directly taxed.
9. Unlimited personal liability of the partners for the firm's debts and liabilities are one of the disadvantages of a general partnership.
10. A corporation is a tax-reporting, not a tax-paying entity.
11. Corporations are separate and distinct from their owners.
12. While pass-through taxation is an advantage, a limited personal liability is a disadvantage.
13. Transferable ownership, raising funds through sale of stock and the ability of continuing indefinitely are the legal benefits of incorporation.
14. The partnership is formed by an agreement entered into by each partner for whom it is advisable to have a written agreement drawn up between all parties.
15. C corporations are pass-through tax entities.
16. S corporations file an informational federal return (Form 1120S), but no income tax is paid at the corporate level.
17. The Board of Directors governs the organization by establishing broad policies and objectives.
18. Many businesses are formed as business trusts to mitigate taxation.

19. A limited partnership, S corporation, and a limited liability company are hybrids, with characteristics of proprietorship, partnership, and corporation.

20. The LLC is a hybrid between a partnership and a corporation, combining the limited liability advantage of a corporation with the tax status of a sole proprietor or partnership.

### 13.5 Language practice

#### 13.5.1 Match the English terms in the left-hand column with the definition in the right-hand column.

1	Pass-through taxation	A	Any technique to multiply gains and losses.
2	Ownership liability	B	A separate legal entity, an LLP provides liability protection for all general partners as well as management rights in the business.
3	S corporations	C	Probability of loss arising from the buyer's reneging on the contract, as opposed to the buyer's inability to pay.
4	Tort	D	unincorporated business organization
5	Professional corporations	E	separately taxable entities
6	Nonprofit corporation	F	pass-through tax entities
7	Memorandum of association	G	A state chartered organization which acts as a separate legal entity and is the most structured business entity.
8	Limited liability partnership	H	The extent to which the owners of a business are liable for the debts of the company.
9	Limited partnership	I	Tax due both on any salary drawn from the corporation and from any

			dividends received from the corporation.
10	Leverage	J	A body of elected or appointed members who jointly oversee the activities of a company or organization.
11	Contract risk	K	company formation
12	Corporation	L	A legal entity that is formed as a non stock corporation with the intent to not realize a profit.
13	C corporations	M	A separate legal entity, this type of business includes a general partner and one or more limited partners who invest capital into the partnership, but do not take part in the daily operation or management of the business.
14	Incorporation	N	Method in which a firm's owners pay income tax on the firm's income and not the firm.
15	Business trust	O	The document that governs the relationship between the company and the outside.
16	Board of Directors	P	a civil wrong
17	Personal income tax	Q	Corporate entities for which many corporation statutes make special provision, regulating the use of the corporate form by licensed professionals.

**13.5.2 Complete the following texts using the suitable words or phrases from the box.**

**Text 1**

<b>A</b>	debts	<b>E</b>	unlimited liability
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<b>B</b>	partnership	<b>F</b>	enterprise
<b>C</b>	legal entities	<b>G</b>	risks and profits
<b>D</b>	limited liability	<b>H</b>	legal action

### Partnerships and Sole Traders

A partnership is a business arrangement in which several people work together, and share \_\_\_\_ (1) \_\_\_\_\_. In Britain and the US, partnerships do not have \_\_\_\_ (2) \_\_\_\_\_ for debts, so the partners are fully liable for any \_\_\_\_ (3) \_\_\_\_\_ the business has. Furthermore, partnerships are not \_\_\_\_ (4) \_\_\_\_\_, so in case of a \_\_\_\_ (5) \_\_\_\_\_, it is the individual partners and not the \_\_\_\_ (6) \_\_\_\_\_ that is taken to court. In most continental European countries there are various kinds of partnership which *are* legal entities.

A sole trader business is an \_\_\_\_ (7) \_\_\_\_\_ owned and operated by a single person who has \_\_\_\_ (8) \_\_\_\_\_ for debts.

### 13.5.3 Complete the text. Replace the Russian words and phrases by the English equivalents.

#### Limited Liability

A company is a business that is a *юридическое лицо*. In other words, it has a *юридическое право на самостоятельное образование от своих владельцев*, the *акционеры*. It can *заключать контракты*, and can *отвечать по иску в суде* if it *нарушит контракт*. A company *имеет непрерывность существования*, even if the *работники и владельцы* change. Most companies have *ограниченная ответственность*, which means that the owners *не нести ответственности* for the business's debts. These companies are known as *компании с ограниченной ответственностью*. Their liability *ограничена стоимостью их акционерного капитала*. The limitation of liability *стимулирует инвесторов* to risk their money to become *владельцами долей компании*, while leaving the *управление* of these companies to *квалифицированным менеджерам высшего руководящего состава*, known as executive directors.

### **13.5.4 Text for discussion.**

*a. Look up the dictionary or Unit 13 Glossary for the meaning and pronunciation of the following words and word-combinations and use them to discuss the problems outlined in the text.*

Sole trader; The Partnership Act of 1890; unanimity; majority vote; precluded by size.

*b. Briefly scan the text and outline the list of major points.*

*c. Read the text more carefully and comment on the following items:*

- the common features of a sole trader and a partnership;
- the main provisions of The Partnership Act of 1890;
- the difference between private companies and public companies;
- the disadvantages of a company as opposed to partnerships and sole traders.

### **Forms of Business Organization in the UK**

Firms can be of different types and sizes. The sole trader is the simplest form of business unit and tends to be found in industries where personal service is important, where there are few advantages in large scale production and where little capital is needed to start up the business. The sole trader provides the capital to run the business, bears the risk of loss, enjoys the benefit of any profits and makes his or her own decisions. There are few legal formalities necessary to start business as a sole trader.

As a form of organization partnerships are commonly found in those professions (such as accountants and solicitors) whose rules may prevent members from forming companies. Many of the problems associated with sole proprietorship may be overcome by forming a partnership. Thus responsibility for finance, risk and work is shared. Unlike companies, partnerships are not a legal entity. This means they cannot own property or sue or be sued in their own name. Like sole traders partners have unlimited liability for the debts of the firm. In

practice this means that partners are legally responsible for both their own and their co-partners' actions. They must choose their partners with care. The Partnership Act of 1890 lays down that

- partners will share profits and losses equally
- decisions relating to the partnership business require unanimity
- decisions relating to the day-to-day running of the business may be settled by majority vote
- all partners are entitled to be involved in the management of the business.
- There are over 1.3 mln companies registered in the UK. They vary in size from the very small with only 2 shareholders to the very large multi-national enterprise in which thousands of shareholders have invested. Companies can be private and public.

Any registered company is deemed to be a private company unless:

- the memorandum of association states that the company is a public limited company and the name includes those words (or the abbreviation plc)
- the memorandum must conform to the requirements of the Companies Acts
- the company has a minimum share capital of 50,000 pounds sterling

As opposed to public companies private companies cannot advertise the sale of their shares or obtain a stock exchange listing. Compared with sole traders and partnerships, companies have the following advantages:

- incorporation creates a new legal entity, independent of its shareholders.
- shareholders have limited liability, thus they know in advance that their liability is limited to the amount they have invested.
- the company has continuity of existence and is unaffected by the death of one of its members.
- it has greater opportunities for raising capital for expansion.

However against these advantages must be put a number of possible disadvantages:



- there is a legal obligation to disclose certain information; for example contractual powers, rules relating to the internal conduct of the business or annual reports
- there may be a divorce between ownership and control
- internal procedures may prevent the company from adapting quickly to changed market conditions
- close relationships between the company, its customers and employees are often precluded by size.

**13.6 Render the passage in English using the English equivalents of the italicized phrases given in Russian. Express the main idea of the passage in one sentence.**

В частной акционерной компании в Англии может состоять от двух до пятидесяти членов. Частная компания не должна направлять бухгалтерские отчеты в *бюро по регистрации акционерных компаний (Registrar)*, но ежегодно заявляет туда о том, что она не предлагала общественности свои акции или облигации. Частная компания – это зачастую дело семейное, капитал для которого собран членами семьи, которые, вследствие этого, владеют акциями компании. Акции могут передаваться другим лицам только с согласия правления компании. Это большой недостаток для держателя акций частных компаний. Так как каждая акция дает право на один голос, акционер должен иметь не менее 51% акций, чтобы получить большинство голосов, необходимое для права передачи акций другому лицу. Акции публичной компании с ограниченной ответственностью могут свободно продаваться на бирже или в ходе частных переговоров.

**Glossary**

**ARTICLES OF ASSOCIATION:** The term articles of association of a company, or articles of incorporation, of an American or Canadian Company, are often simply referred to as articles (and are often capitalized as an abbreviation for the full term). The Articles are a

requirement for the establishment of a [company](#) under the law of [India](#), the [United Kingdom](#) and many other countries. Together with the [memorandum of association](#), they are the constitution of a company. The equivalent term for [LLC](#) is [Articles of Organization](#).

The Articles can cover a medley of topics:

- the issuing of [shares](#) (also called [stock](#)), different voting rights attached to different classes of shares
- valuation of intellectual rights, say, the valuations of the IPR of one partner and, in a similar way as how we value real estate of another partner
- the appointments of directors - which shows whether a shareholder dominates or shares equality with all contributors
- directors meetings - the quorum and percentage of vote
- management decisions - whether the board manages or a founder
- transferability of shares - assignment rights of the founders or other members of the company do
- special voting rights of a Chairman, and his/her mode of election
- the [dividend policy](#) - a percentage of profits to be declared when there is profit or otherwise
- winding up - the conditions, notice to members
- confidentiality of know-how and the founders' agreement and penalties for disclosure
- first right of refusal - purchase rights and counter-bid by a founder.

A Company is essentially run by the shareholders, but for convenience, and day-to-day working, by the elected Directors. Usually, the shareholders elect a Board of Directors (BOD) at the Annual General Meeting (AGM).

**BOARD OF DIRECTORS:** A body of elected or appointed members who jointly oversee the activities of a company or organization. Other names include **board of governors**, **board of managers**, **board of regents**, **board of trustees**, and **board of visitors**. It is often simply referred to as "the board". In some European Union and Asian countries, there are two separate boards, an executive board, also called *corporate executive team*, for day-to-day business and a **supervisory board**, also called *board of*

*directors* (elected by the shareholders) for supervising the executive board. A board's activities are determined by the powers, duties, and responsibilities delegated to it or conferred on it by an authority outside itself. These matters are typically detailed in the organization's bylaws. The bylaws commonly also specify the number of members of the board, how they are to be chosen, and when they are to meet. In an organization with voting members, *e.g.*, a professional society, the board acts on behalf of, and is subordinate to, the organization's full assembly, which usually chooses the members of the board. In a stock corporation, the board is elected by the stockholders and is the highest authority in the management of the corporation. In a non-stock corporation with no general voting membership, *e.g.*, a university, the board is the supreme governing body of the institution; its members are sometimes chosen by the board itself. Typical duties of boards of directors include:

- governing the organization by establishing broad policies and objectives;
- selecting, appointing, supporting and reviewing the performance of the chief executive;
- ensuring the availability of adequate financial resources;
- approving annual budgets;
- accounting to the stakeholders for the organization's performance;
- setting the salaries and compensation of company management.

The legal responsibilities of boards and board members vary with the nature of the organization, and with the jurisdiction within which it operates. For public corporations, these responsibilities are typically much more rigorous and complex than for those of other types. Typically the board chooses one of its members to be the *chairman*, who holds whatever title is specified in the bylaws.

**BUSINESS TRUST:** A **Massachusetts business trust (MBT)** is a legal [trust](#) set up for the purposes of business, but not necessarily one that is operated in [the commonwealth of Massachusetts](#). They may also be referred to as an **unincorporated business organization** or **UBO**. Business trusts may be established under the laws of other U.S. states.

Many businesses are formed as MBTs to mitigate taxation; [mutual funds](#) in the U.S. are often structured as MBTs, though sometimes they are organized as Maryland corporations (or other states such as

Minnesota). More recently, a [Delaware statutory trust](#) or *DST* has become a popular form of organization, and many new funds have been organizing as DSTs and exiting funds converting to DSTs. Since mutual funds are [investment companies](#) and not operating companies, many traditional corporation rules and requirements don't fit them well.

**COMPANY FORMATION:** In the U.K., the process of incorporation is generally called company formation. The United Kingdom is one of the quickest locations to incorporate, with a fully electronic process and a very fast turnaround by the national registrar of companies, the [Companies House](#). The current [Companies House](#) record is five minutes to vet and issue a [certificate of incorporation](#) for an electronic application.

**CORPORATION:** This state chartered organization acts as a separate legal entity and is the most structured business entity. Business activities are restricted to those listed in the corporate charter. Corporations may elect to file as a C-Corporation or S-Corporation. The differences are defined by the tax filing status as determined by the chapters in the Internal Revenue Code.

**C CORPORATION:** C corporations are separately taxable entities. They file a corporate tax return (Form 1120) and pay taxes at the corporate level. They also face the possibility of double taxation if corporate income is distributed to business owners as dividends, which are considered personal income. Tax on corporate income is paid first at the corporate level and again at the individual level on dividends.

**C CORPORATION VS S CORPORATION:** C corporation is the standard corporation, while the S corporation has elected a special tax status with the IRS. It gets its name because it is defined in Subchapter S of the Internal Revenue Code. To elect S corporation status when forming a corporation, Form 2553 must be filed with the IRS and all S corporation guidelines met. C corporations and S corporations share many qualities:

- **Limited liability protection.** Both offer limited liability protection, so shareholders (owners) are typically not personally responsible for business debts and liabilities.

- **Separate entities.** Both the S corporation and C corporation are separate legal entities created by a state filing.
- **Filing documents.** Formation documents must be filed with the state. These documents, typically called the Articles of Incorporation or Certificate of Incorporation, are the same for both C and S corporations.
- **Structure.** Both have shareholders, directors and officers. Shareholders are the owners of the company and elect the board of directors, who in turn oversee and direct corporation affairs and decision-making but are not responsible for day-to-day operations. The directors elect the officers to manage daily business affairs.
- **Corporate formalities.** Both are required to follow the same internal and external corporate formalities and obligations, such as adopting bylaws, issuing stock, holding shareholder and director meetings, filing annual reports, and paying annual fees.

#### **S corporation vs. C corporation: The differences**

Despite their many similarities, S corporations and C corporations also have distinct differences.

- **Taxation.** Taxation is often considered the most significant difference for small business owners when evaluating S corporations vs. C corporations.

**CONTRACT RISK:** It is probability of loss arising from the buyer's reneging on the contract, as opposed to the buyer's inability to pay. It is probability of loss arising from failure in contract performance. Vendors have the highest risk in fixed price contracts and least in the cost type contracts.

**CORPORATE OWNERSHIP:** C corporations have no restrictions on ownership, but S corporations do. S corps are restricted to no more than 100 shareholders, and shareholders must be US citizens/residents. S corporations cannot be owned by C corporations, other S corporations, LLCs, partnerships or many trusts. Also, S corporations can only have one class of shares.

**GENERAL PARTNERSHIP:** Allows two or more people to share profits and liabilities. A general partnership is similar to a sole proprietorship, except that two or more parties are involved. In a business partnership, the parties that join forces could be individuals,

corporations, trusts, other partnerships, or a combination of all of the above.

- **Advantages:** Advantages are that it is easy to establish, can draw upon the financial and managerial strength of all the partners, and the profits are not directly taxed.
- **Disadvantages:** Some disadvantages are unlimited personal liability of the partners for the firm's debts and liabilities, termination of the business with the death of a partner (in the absence of advanced planning for business continuation) and the fact that any one of the partners can commit the firm to obligations. It is important to understand that a general partnership does not protect its partners from personal liability with respect to claims against the partnership. The partnership is formed by an agreement entered into by each partner. This agreement may be informal, but it is advisable to have a written agreement drawn up between all parties.

**LEGAL BENEFIT OF INCORPORATION:** Protection of personal assets. One of the most important legal benefits is the safeguarding of personal assets against the claims of creditors and lawsuits. Sole proprietors and general partners in a partnership are personally and jointly responsible for all the liabilities of a business such as loans, accounts payable, and legal judgments. In a corporation, however, stockholders, directors and officers typically are not liable for the company's debts and obligations. They are limited in liability to the amount they have invested in the corporation. For example, if a shareholder purchased \$100 in stock, no more than \$100 can be lost. Corporations and limited liability companies (LLCs) may hold assets such as real estate, cars or boats. If a shareholder of a corporation is personally involved in a lawsuit or bankruptcy, these assets may be protected. A creditor of a shareholder of a corporation or LLC cannot seize the assets of the company. However, the creditor can seize ownership shares in the corporation, as they are considered a personal asset.

- Transferable ownership. Ownership in a corporation or LLC is easily transferable to others, either in whole or in part. Some state laws are particularly corporate-friendly. For example, the transfer

of ownership in a corporation incorporated in Delaware is not required to be filed or recorded.

- Retirement funds. Retirement funds and qualified retirements plans, such as a 401(k), may be established more easily.
- Taxation. In the United States, corporations are taxed at a lower rate than individuals are. Also, they can own shares in other corporations and receive corporate dividends 80% tax-free. There are no limits on the amount of losses a corporation may carry forward to subsequent tax years. A sole proprietorship, on the other hand, cannot claim a capital loss greater than \$3,000 unless the owner has offsetting capital gains.
- Raising funds through sale of stock. A corporation can easily raise capital from investors through the sale of stock.
- Durability. A corporation is capable of continuing indefinitely. Its existence is not affected by the death of shareholders, directors, or officers of the corporation.
- Credit rating. Regardless of an owner's personal credit scores, a corporation can acquire its own credit rating, and build a separate credit history by applying for and using corporate credit.

**LEGAL TYPES:** The three primary types of legal firm organizations are: (1) proprietorship, (2) partnership, and (3) corporation. One primary difference between these three legal types are number of owners -- proprietorship has one, partnership has two or more (but usually a small number), and corporation can have anywhere from one or to millions. A second difference is the liability of the owners -- proprietorship and partnership owners have unlimited liability and corporation owners have limited liability. Three newer firm types include (1) limited partnership, (2) S corporation, and (3) limited liability company. Each of these three are hybrids, with characteristics of proprietorship, partnership, corporation.

**LEVERAGE:** In finance, leverage (sometimes referred to as **gearing** in the United Kingdom, or **solvency** in Australia) is a general term for any technique to multiply gains and losses. Common ways to attain leverage are borrowing money, buying fixed assets and using derivatives. The examples could be:

- A public corporation may leverage its equity by borrowing money. The more it borrows the less equity capital it needs, so any profits or losses are shared among a smaller base and are proportionately larger as a result.
- A business entity can leverage its revenue by buying fixed assets. This will increase the proportion of fixed, as opposed to variable, costs, meaning that a change in revenue will result in a larger change in operating income.
- Hedge funds often leverage their assets by using derivatives. A fund might get any gains or losses on \$20 million worth of crude oil by posting \$1 million of cash as margin.

**LIMITED LIABILITY COMPANY:** A separate legal entity, the LLC is a hybrid between a partnership and a corporation, combining the limited liability advantage of a corporation with the tax status of a sole proprietor or partnership. Owners of the LLC are called members.

- **Advantages:** Similar to the partnership entities, the LLC is governed by an operating agreement, or in the absence of one, by the Connecticut Limited Liability Company Act. The LLC may be formed by one or more members. As a separate legal entity, LLC's may own property, sue, and be sued in LLC's name. Managers of an LLC as elected by the members may be in the form of a person or other entity. Unless otherwise specified by the Articles of Organization, LLC's enjoy perpetual continuity similarly as in a corporation.
- **Disadvantages:** Since a LLC is a legal entity, the formation of a LLC requires more legal documentation than in a general partnership or sole proprietorship

**LIMITED PARTNERSHIP:** separate legal entity, this type of business includes a general partner and one or more limited partners who invest capital into the partnership, but do not take part in the daily operation or management of the business. The limited partners limit their amount of liability to the amount of capital invested in the partnership. The general partner shoulders the personal liability for the debts and obligations of the partnership. Business operations are governed, unless otherwise specified in a written agreement, by majority vote of



voting partners. LPs are legal entities formed with the Connecticut Secretary of the State.

- **Advantages:** LPs provide a legal structure to the establishment of the business. From a capital investment standpoint, limited partners are shielded from the liability in that their liability is dependent upon the amount of capital invested. In addition, dividends distributed to all partners are reported on the partners' personal income tax return. There are no restrictions as to the amount of dividends that the general partners may receive from the business. General partners of a LP may be in the form of another person or company. As a separate legal entity, LP's may own property, sue, and be sued in LP's name.
- **Disadvantages:** In a LP there must be at least one general partner and it is the general partner(s) that incur unlimited liability. As in any partnership, a LP must draft a partnership agreement, which governs how the business is operated. In a LP the partnership agreement must state a date of termination. Since a LP is a legal entity, the formation of a LP requires more legal documentation than in a general partnership.

**LIMITED LIABILITY PARTNERSHIP:** A separate legal entity, an LLP provides liability protection for all general partners as well as management rights in the business. Most commonly used in professional practices, an LLP offers, in most cases, the same limited liability enjoyed by a corporation, but at the same time it is a flow-through entity for federal and Connecticut tax purposes, just like a partnership. LLP's are legal entities formed with the Connecticut Secretary of the State.

- **Advantages:** LLP's provide a legal structure to the establishment of the business. From a capital investment standpoint, limited partners are shielded from the liability in that their liability is dependent upon the amount of capital invested. In addition, dividends distributed to all partners are reported on the partners' personal income tax return. As in any partnership, a LLP must draft a partnership agreement, which governs how the business is operated. There is no requirement to set a termination date of the partnership agreement. As a separate legal entity, LLP's may own property, sue, and be sued in LLP's name.
- **Disadvantages:** Since a LLP is a legal entity, the formation of a LLP requires more legal documentation than in a general partnership. If a

LLP drops or loses a partner, the business is automatically deemed dissolved.

**MEMORANDUM OF ASSOCIATION:** The memorandum of association of a [company](#), often simply called the memorandum (and then often capitalized as an abbreviation for the official name, which is a proper noun and usually includes other words), is the document that governs the relationship between the company and the outside. It is one of the documents required to incorporate a [company](#) in the United Kingdom, Ireland, India, Bangladesh, Pakistan and Sri Lanka, and is also used in many of the [common law jurisdictions](#) of the [Commonwealth](#).

**NONPROFIT CORPORATION:** A nonprofit corporation is a legal entity that is formed as a non stock corporation with the intent to not realize a profit, but is established for a religious, charitable, educational, literary or scientific purpose. Qualifying nonprofit corporations will be granted tax-exempt status by both federal and state authorities.

**OWNERSHIP AND CONTROL:** Ownership means that you have legal "title" to a resource, good, or commodity. Control means that you have the ability to determine how a resource, good, or commodity is used. While it would seem as though these two always go together, such is not the case. People generally have ownership and control over their labor and personal property (clothing, furniture, canned goods, etc.). But in some circumstances ownership is absent of control and control exists without ownership.

**OWNERSHIP LIABILITY:** The extent to which the owners of a business are liable for the debts of the company. The two basic liability alternatives are unlimited liability, which has no restrictions on ownership liability, and limited liability, which does have restrictions. Ownership liability is one characteristic separating legal business organizations. Proprietorships and partnerships have unlimited liability. Corporations have limited liability.

**PASS-THROUGH TAXATION:** Method in which a firm's owners pay income tax on the firm's income and not the firm.

**PERSONAL INCOME TAXES:** With both types of corporations, personal income tax is due both on any salary drawn from the corporation and from any dividends received from the corporation.

**PROFESSIONAL CORPORATIONS:** are those corporate entities for which many [corporation](#) statutes make special provision, regulating the use of the corporate form by licensed professionals such as [attorneys](#), [architects](#), [engineers](#), public [accountants](#) and [physicians](#). Legal regulations applying to professional corporations typically differ in important ways from those applying to other corporations. Professional corporations, which may have a single director or multiple directors, do not usually afford that person or persons the same degree of limitation of liability as ordinary business corporations ([cf. LLP](#)). Such corporations must identify themselves as professional corporations by including "PC" or "P.C." after the firm's name. Professional corporations often exist as part of a larger, more complicated, legal entity; for example, a [law firm](#) or [medical practice](#) might be organized as a partnership of several or many professional corporations

**S CORPORATIONS:** S corporations are pass-through tax entities. They file an informational federal return (Form 1120S), but no income tax is paid at the corporate level. The profits/losses of the business are instead “passed-through” the business and reported on the owners’ personal tax returns. Any tax due is paid at the individual level by the owners.

**SOLE PROPRIETORSHIP:** A sole proprietorship by definition means "one owner". The owner assumes all responsibilities for the business, including assets and liabilities. Business income is taxed as personal income. Most small businesses operate as sole proprietorships, this being the simplest form of organization and allowing the single owner to have sole control and responsibility. The business may use a trade name, but the business does not have a separate legal existence apart from its owner under state law. Trade names (often referred to as fictitious names, DBA or doing business as) must register with the town or city clerk in the town or city where the business is located.

- **Advantages:** Some advantages of the sole proprietorship are less paperwork, minimal legal restrictions, owner retention of all profits, and ease in discontinuing the business. In most cases, a sole proprietorship is not required to obtain an Employer Identification Number (EIN) from the Internal Revenue Services unless it has employees. There is no need to file a separate income tax return for the proprietorship because the activity is reported on the owner's federal and individual income tax returns. Since a self-employed person is not considered an employee, there is no provision to withhold payroll taxes to cover federal, state, and Social Security tax obligations. If you are a self-employed sole proprietor, you must make quarterly estimated payments to provide for these tax liabilities.
- **Disadvantages:** Disadvantages include unlimited personal liability for all debts and liabilities of the business, limited ability to raise capital, and termination of the business upon the owner's death. You should note that a small business owner might very well select the sole proprietorship to begin, and later, he or she may decide to form a different business type such as a limited liability company or corporation.

**TAX RETURN:** Tax returns in the [United States](#) are reports filed with the [Internal Revenue Service](#) (IRS) or with the state or local [tax](#) collection agency ([California Franchise Tax Board](#), for example) containing information used to calculate [income tax](#) or other taxes. Tax returns are generally prepared using [forms](#) prescribed by the IRS or other applicable taxing authority.

**TORT:** A tort, in [common law](#) jurisdictions, is a [civil wrong](#). Tort law deals with situations where a person's behavior has unfairly caused someone else to suffer loss or harm. A tort is not necessarily an illegal act but causes harm and therefore the law allows anyone who is harmed to recover their loss. Tort law is different to [criminal law](#), which deals with situations where a person's actions cause harm to society in general. A claim in tort may be brought by anyone who has suffered loss. Criminal cases tend to be brought by the state, although [private prosecutions](#) are possible.

