

# Factors in Selecting Business Form

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## **I. Preliminary Considerations**

### **A. General Client Information**

Has the following information been collected regarding each of the principals who are to be involved in the proposed venture:

- (1) Name and address;
- (2) Present business occupation;
- (3) Business background and experience;
- (4) Marital status and related agreements;
- (5) Estate planning arrangements;
- (6) Financial information.

### **B. General Information Regarding Proposed Business**

Has the following information been collected regarding the proposed business:

- (1) Description of the proposed product(s) or service(s);
- (2) Inventions involved in the proposed business;
- (3) Present or proposed management structure for the business;
- (4) Production and distribution plans;
  
- (5) Market conditions;
- (6) Potential liabilities associated with the proposed business.

### **C. Client's Business and Personal Objectives**

What are the client's business and personal objectives with respect to the proposed business activities?

### **D. Capitalization**

How will the capital necessary for formation and operation of the business be obtained?

Consider the personal assets of the proposed owners and outside sources of capital, including passive investors and commercial lenders.

### **E. Compensation and Profit Distribution**

How will the revenues from the business be distributed among the owners and employees?

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### **F. Non-Tax Business Organizations**

Has the client been advised of the various non-tax forms of business organization?

### **G. Organizational Forms for Tax Purposes**

Has the client been advised of the various forms of business organization which are recognized under the tax laws?

### **II. Legal Considerations**

Are there any legal limitations on the choice of business form?

### **III. Non-Tax Considerations**

#### **A. Advantages of Non-Corporate Entities**

Has the client been advised of the non-tax advantages of conducting business in one of the non-corporate forms of business organization?

#### **B. Disadvantages of Non-Corporate Entities**

Has the client been advised of the possible non-tax disadvantages of conducting business in one of the non-corporate forms of business organization?

#### **C. Advantages and Disadvantages of Corporate Entities**

Has the client been advised of the possible non-tax advantages and disadvantages of conducting business in the corporate form?

#### **D. Liabilities Associated with Business Activities**

Are there concerns regarding the possibility that the activities of the business will result in personal liability to the owners in excess of the amounts actually contributed to the business?

#### **E. Capital Requirements**

Is it likely that the venture will require outside financing in the near future?

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### **F. Centralized Management**

Is centralized management of the business desired?

### **G. Utility of Ownership Interests**

How effective are ownership interests in the entity in recruiting key employees and achieving liquidity for the holder?

### **H. Continuity of Life**

Is continuity of life desirable?

### **I. Administrative Complexity and Expense**

Has the client considered the administrative complexity and expense associated with each of the organizational forms?

### **J. Hybrid Forms of Organization**

Would a hybrid form of organization satisfy the needs of the client?

### **K. State of Organization**

Assuming selection of an appropriate form of business organization, should the clients organize the entity in a state other than the state in which they reside and/or the principal activities of the business are to be conducted?

## **IV. Tax Considerations**

### **A. Advantages and Disadvantages of Non-Corporate Entities**

Has the client been advised of the various tax advantages and disadvantages of conducting business in one of the non-corporate forms of business organization?

### **B. Advantages of Using the Corporate Form**

Has the client been advised of the various tax advantages of conducting business in the corporate form?

### **C. Losses**

Will the venture generate tax losses in early years?

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### **D. Taxation of Income**

Should income be taxed to the participants or should it be taxed to a separate entity? If the latter, how is the double taxation problem to be minimized?

### **E. Compensation Arrangements**

What effect will the choice of entity for tax purposes have on the ability of the business to select and structure appropriate compensation arrangements for its owners and employees?

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#### **About the Author:**

Ms. Sharmil McKee is a business attorney licensed in Pennsylvania. She focuses her practice on protecting small and mid-sized businesses from future legal problems. Visit her firm's website <http://www.mckeeoffice.com>.