S Corporation Election Considerations for Corporations and LLCs
Nellie Akalp, CorpNet CEO:

Nellie Akalp is an entrepreneur, business expert, professional speaker, published author, and mother to four amazing kids. Nellie has dedicated her entrepreneurial career to helping other entrepreneurs and business professionals succeed at business ownership.

As CEO and Co-Founder of CorpNet.com, she has helped more than half a million small businesses and licensed professionals get their businesses and clients off the ground. She has developed a strong following within the small business community and has been honored as a Small Business Influencer Champion and was named women entrepreneur of the year by NAWBO.
Today’s Agenda

Goal: Understand how the S Corporation election differs for Corporations, LLCs, and within various states.

- What is the S Corporation
- S Corporation treatment for Corporations
- S Corporation treatment for LLCs
- S Corporation Election at the State Level
- How to Become an S Corporation
- 2020 S Corporation Election Deadlines
- Operating as an S Corporation
The S Corporation
What is the S Corporation?

- Not a type of business entity
- Special tax election for eligible Limited Liability Companies (LLCs) or Corporations
- Business owners must decide whether a company will be registered as LLC or Corporation before electing S Corporation treatment
- IRS has issued eligibility requirements for S Corporation status
Understanding the Difference

The potential advantages of electing S Corporation tax treatment are a bit different for LLCs and Corporations.

- Crucial to consider the differences when deciding whether to form an LLC or Corporation to obtain S Corporation status.
- Critical to understand the differences between the LLC and Corporation business entity types.
- Aside from tax implications, there are legal and administrative factors to consider.
S Corporation Treatment for Corporations
Corporations and the S Corporation Election

Overview of a Corporation

- Separate legal and tax-paying entity
- Highest level of protection
- Can sell company stock and offer stock options
- Unlimited number of shareholders
# Corporations and the S Corporation Election

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## Starting and Running a Corporation
- More involved and costly than forming an LLC
- Several legal steps to get started
- Comply with ongoing compliance and tax requirements
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- Profits & losses flow through to corporate tax return
- Taxable income taxed at corporate rate
- Some businesses undergo double-taxation
- Dividends to shareholders not tax-deductible

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### S Corporation Tax Treatment for Corporations
- Avoid double-taxation
- Profits & losses flow through to shareholders’ personal tax return
- Corporation itself does not pay income tax
Does an S Corporation Election Make Sense for Your Clients’ Corporation?

- It can depend on client’s business goals. If the plan is to sell the business, forming a Corporation and electing S Corporation status could be a benefit.

- If your client has a business in a dangerous industry, a corporate formation is a better idea due to higher legal protection.

- A Corporation with S Corporation election benefits small businesses where the shareholders want greater liability protection, want to be on payroll and take out a reasonable salary, and do not want to be taxed twice.
S Corporation Treatment for Limited Liability Companies (LLCs)
LLCs and the S Corporation Election

Overview of an LLC

- Separate legal entity
- Liability protection
- Less rigid compliance requirements
LLCs and the S Corporation Election

<table>
<thead>
<tr>
<th>Overview of an LLC</th>
<th>Starting and Running an LLC</th>
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<tbody>
<tr>
<td>○ Separate legal entity</td>
<td>○ Affordable and ‘simple’ to file</td>
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<tr>
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# LLCs and the S Corporation Election

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## Default Tax Treatment of LLCs
- IRS does not consider separate tax-paying entity
- Pass-through entity
- Subject to self-employment tax
LLCs and the S Corporation Election

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- Separate legal entity
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Default Tax Treatment of LLCs
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S Corporation Tax Treatment for LLCs
- Reduce self-employment tax
- Salary must be fair compensation or red flag for IRS
- More flexible than C Corporation option
Does an S Corporation Election Make Sense for Your Clients’ LLC?

- If your client is looking to avoid many formalities of a Corporation - Minutes, Board of Directors, Annual Meetings, etc - an LLC with S Corporation election would be a good fit.
- If a client is looking to stay in business long-term, an LLC with S Corporation election could be a wise choice.
- An LLC owner that elects to file as an S Corporation would take payroll instead of guaranteed payments, limiting self-employment tax. This could be appealing to many clients.
- Forming an LLC with S Corporation election is a wise choice if your client intends to file as a partnership or sole-proprietor in the future.
Weighing Options

- Clients in the Real Estate industry should typically operate as an LLC due to distributing property to the individuals tax free, but it is a taxable event if distributed through an S Corporation.

- Talk with your client about how they want to present their company publicly. Having an ‘LLC’ vs an ‘Inc’ at the end of a business name can make an impact, however, this does not change based on how taxes are filed.

- If you and your client are unsure about the best option, consider forming an LLC. You can always incorporate later. However if you incorporate first and later decide an LLC is best, a lot more work is involved.
S Corporation Election at the State Level
Many States Have Different Rules

- S Corporation election benefits can change at the state vs federal level
- Most states are given S Corporation pass-through tax treatment, but there are exceptions
- Critical that clients understand how this affects their business
State-Level S Corporation Election Requirements

New Jersey
State-level S Corporation tax treatment requires filing Form CBT-2553. The state will only consider the election valid if all of a corporation’s shareholders consent to the election and other state requirements.
State-Level S Corporation Election Requirements

New York

New York state does not automatically treat a company as a New York S Corporation unless mandated to file as an S Corporation under Tax Law section 660(i).

New York requires a corporation to file form CT-6 to apply for S Corporation tax treatment at the state level.
State-Level S Corporation Election Requirements

Arkansas

It was not until 2018 that Arkansas recognized S Corporation tax treatment at the state level without additional paperwork.

Make sure clients are aware of this new change!
Utah
Utah requires a copy of a company’s Notice of Acceptance as an S Corporation from the IRS. The notice must be attached to Form TC-20S the first time the company files its tax return.
Where S Corporation Flow-Through Tax Treatment Does Not Exist

Some jurisdictions do not recognize S Corporation election. Tax agencies in the following areas do not grant pass-through taxation for corporations that have been approved for federal S Corporation tax treatment.

<table>
<thead>
<tr>
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<tr>
<td>District of Columbia</td>
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<tr>
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<tr>
<td>New Hampshire</td>
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<tr>
<td>New York City</td>
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<tr>
<td>Tennessee</td>
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<tr>
<td>Texas</td>
</tr>
<tr>
<td>California</td>
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</tbody>
</table>
States Without Personal or Corporate Income Taxes

S-Corporation election is essentially a non-issue in some areas as there are no state income taxes at the personal or corporate level. Note: some of these states, however, may enforce other types of fees to an S Corporation or its shareholders.

- Alaska
- Florida
- Nevada
- South Dakota
- Washington
- Wyoming

*Not comprehensive list. Info subject to change at the state level*
How to Become an S Corporation
Eligibility

To qualify for S Corporation status, a Corporation or LLC must meet the following requirements:

- Be a domestic corporation
- Have only allowable shareholders
  - May be individuals, certain trusts, and estates and
  - May not be partnerships, corporations or non-resident alien shareholders
- Have no more than 100 shareholders
- Have only one class of stock
- Not be an ineligible Corporation - certain financial institutions, insurance companies, and domestic international sales corporations
- Form 2553 signed by all shareholders and submitted
Filing as a Corporation vs LLC

Both a Corporation and an LLC file for S Corporation treatment the same.

File IRS Form 2553 with the IRS.

The election must be made no more than two months and 15 days after the beginning of the tax year when the election goes into effect.
2020 S Corporation Election Deadline

For S Corporation tax treatment to be in effect for 2020, existing businesses must meet the IRS deadline of **March 16, 2020** to file Form 2553. Missing the deadline means the business will continue to be taxed as a C Corporation or LLC for the remainder of the 2020 tax year, with S Corporation treatment starting January 1, 2021.

Newly formed LLCs and Corporations have **two months and 15 days (75 days)** from their date of formation to file for S Corporation election for the tax year 2020.

Business owners can request a six-month **extension** to file for S Corporation status by filing IRS Form 7004.
What if the S Corporation Deadline is Missed?

If a Corporation or LLC fails to timely file its IRS form 2553 with the IRS, the S Corporation election will NOT be effective for that year.

A corporation will be taxed as a C Corporation.

A single-member LLC will be taxed as a sole proprietorship and a multi-member LLC will be taxed as a partnership.

A late S Corporation election is generally effective for the next tax year. Relief for late election may be available if the Corporation or LLC can show that the failure to file on time was due to reasonable cause.
Operating as an S Corporation
How Clients Pay Themselves

To avoid red flags for the IRS:

- An S Corporation shareholder who does substantial work for the S Corp is considered an employee of the corporation and must take a reasonable salary from the corporation on payroll.
- The business must put the shareholder on payroll and compensate the shareholder through a reasonable salary - from which taxes are withheld.
- An S Corporations remaining profits are paid out in the form of distributions to the company’s shareholders, who report those distributions on their personal tax returns.
- S Corporation owners can run into trouble if they pay themselves a suspiciously small salary and then take most of their compensation in the form of distributions to minimize the amount of taxes they have to pay.
- The IRS can revoke an S Corporation status if they determine shareholders are substantially underpaid for the services they provide.
## Ongoing Compliance Requirements

<table>
<thead>
<tr>
<th>Type</th>
<th>Initial Filing Requirements</th>
<th>Annual Compliance Requirements</th>
<th>Registered Agent Required</th>
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Our Tools Are Your Resources

Welcome to B.I.Z.!
Your Business Information Zone
The secure, cloud based Corporate Compliance Tool available to EVERYONE... for FREE!

- Corporate / LLC Kit
- Meeting Minutes Templates
- LLC Operating Agreement
CorpNet.com Partner Program

Private Label: Resell CorpNet Services
- Offer business formation and compliance.
- CorpNet is a silent, white labeled partner.
- CorpNet never contacts your client.
- All documents, alerts, and information are sent directly to you without labels.
- You will have a Dedicated Account Manager who knows your specific requirements and is available to you for whatever you need.

Referral Program: Refer Your Clients
- Refer your clients to CorpNet and they will receive white glove treatment.
- A dedicated account manager will work with your clients to ensure a personalized experience and a “hand-off” back to you when the process is complete.
- Earn commissions up to 25% or pass the savings to your client.

Participating in both our Reseller and Referral partner programs is ok!

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