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In which state should my entity be formed?

Choosing The Entity For Your Business



Once you decide to incorporate, the next question is what type of company you should form. Many years ago, business owners formed corporations because that was the only viable choice. Now, there are limited liability companies (LLC), limited partnerships (LP) and limited liability partnerships (LLP) that provide comparable benefits. In addition, there are now "S" Corporations, which are distinguishable from the traditional "C" Corporations. With all of these choices, how does one go about selecting the appropriate form of entity to conduct business?

First, and depending on what you are doing, you may be disqualified from some of the choices. For example, LLCs may not render professional services. There are approximately 150 professional license types in California, from accountants to vocational nurses. Only accountants, architects, and attorneys are allowed to form LLPs.

As another example, you cannot form an S Corporation if any of the shareholders are not U.S. citizens or residents, if there would be more than 100 shareholders, or if any

shareholders would be another corporation.

Assuming that you would be eligible for different choices, then an evaluation of the costs and benefits to each choice becomes necessary. For example, California LLCs are subject to a gross receipts fee (the constitutionality of which is currently being challenged). S Corporations, by contrast, are not subject to a gross receipts fee but are subject to a 1.5% net income tax in California. When choosing between LLCs and S corporations, your accountant should be able to crunch the numbers and advise you as to which entity form should be less costly.

Aside from the tax implications, there are many other factors that could favor one entity. For example, if you intend to raise capital from investors, grant stock options and/or offer certain types of benefits, then a C corporation may make the most sense.

This article only provides some issues that you should consider if you decide to "incorporate." You should consult with an attorney experienced in structuring entities before making your selection. Structure Law Group, LLP has formed many entities. Please contact us at (408) 441-7500 if you are interested in forming an entity.

Success Story



Structure Law Group, LLP formed a corporation for an entrepreneur's first start-up business. We advised the entrepreneur to form a C corporation to accommodate an affiliation with a company in India. We further assisted the client to structure an important transaction with the Indian company. Our client has since been acquired in a multi-million dollar transaction. We helped structure the acquisition as a stock purchase so that our client would not retain liabilities. We also helped our client negotiate for the acquiror to pay for a significant portion of our client's legal fees.

New Procedures For Dissolving Entities In California

For years corporate entities have sweated at year-end trying to ensure that all unneeded corporations, LLCs, LPs and LLPs were dissolved, and a tax clearance certificate was obtained, so that the entity would not owe another \$800 for the next year. If the tax return is not filed in time, or the tax clearance certificate is not obtained within a short period, the entity could have to pay another \$800 and try dissolving again next year. Often, clients have come to us with entities that have not done any business for years, and may even have filed a final tax return years earlier, but failed to formally dis-

solve with the Secretary of State and, therefore, continue to owe \$800 per year, plus penalties and interest if it were not paid on time.

Finally, the Franchise Tax Board has said that effective September 29, 2006, it will no longer assess the \$800 for the next year if three requirements are met:

1. The entity must file a final tax return on or before the extended due date for the preceding tax year;
2. The entity does not conduct business in California after the end of that year; and
3. The entity files a Certifi-

cate of Dissolution, Certificate of Surrender, or Certificate of Cancellation with the Secretary of State before the end of the 12 month period beginning with the date the final return was filed.

This greatly simplifies the dissolution process. There will be no more tax clearance forms, and the Secretary of State has revised the Certificates of Dissolution, Cancellation and Merger to reflect these changes. The old forms are no longer valid.

Unfortunately, no retroactive relief is provided for entities that failed to formally dissolve years ago and have

accumulated taxes, penalties and interest. However, if your entity filed a timely 2005 final tax return, did not conduct business after 2005, filed timely dissolution paperwork with the Secretary of State and paid \$800 for 2006, it may be entitled to a refund. If you want to dissolve an entity that is no longer doing business, contact us to avoid 2007 franchise taxes.

“This greatly simplifies the dissolution process.”

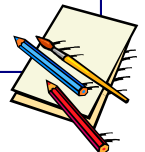


Tax Corner

- **Mileage Rate Increased To 48.5¢.** For 2007 the IRS has increased the standard mileage rate for business driving to 48.5 cents per mile, up from 44.5 cents in 2006. Remember, this is in place of deducting fuel and vehicle repair costs, but parking and tolls are still deductible. [Source: IRS-IR-2006-168, November 1, 2006.]
- **Minimum Wage Increased to \$7.50.** Effective January 1, 2007, California minimum wage has increased from \$6.75 to \$7.50 per hour, and will increase again on January 1, 2008 to \$8 per hour. [AB 1835]
- **Registered Domestic Partners Must File as Married.** Beginning January 1, 2007, Registered Domestic Partners will be required to file as married in California, and all community property rules will apply. [SB 1827, Ch. 6-802.] However, they are still prohibited from doing so on Federal returns, and community property rules are not applicable.

If you have any questions regarding the above changes, please contact Tamara Pow at (408) 441-7500.

Note For Architects: A new law just extended the ability of architects to be Limited Liability Partnerships (LLPs) from January 1, 2007 to January 1, 2012, and increased the minimum liability insurance coverage requirement to \$1,000,000 (plus an additional \$100,000 for each architect over 5) starting January 1, 2008. [AB 2914, Ch. 06-426.]



Are You At Risk For Identity Theft? - Take This Identity Theft IQ Test*



- I receive several offers of pre-approved credit every week. **(5 points)**
- Add 5 points** if you do not shred them before putting them in the trash.
- I carry my Social Security card in my wallet. **(10 points)**
- My state driver's license has my SSN printed on it and I have not contacted the DMV to request a different number. **(10 points)**
- I do not have a PO Box or a locked, secured mailbox. **(5 points)**
- I use an unlocked, open box at work or at my home to drop off my outgoing mail. **(10 points)**
- I do not shred or tear banking and credit information when I throw it in the trash. **(10 points)**
- I provide my SSN whenever asked, without asking questions as to how that information will be safeguarded. **(10 points)**
- Add 5 points** if you provide it orally without checking to see who might be listening.
- I am required to use my SSN at work as an employee ID or at college as a student ID number. **(5 points)**
- My SSN is printed on my employee badge that I wear at work or in public. Or it is posted on my time card in full view of others, or is on other documents frequently seen by many others in my workplace. **(10 points)**
- I have my SSN and/or driver's license number printed on my personal checks. **(10 points)**
- I am listed in a "Who's Who" guide. **(5 points)**
- I carry my insurance card in my wallet and either my SSN or that of my spouse is the ID number. **(10 points)**
- I have not ordered a copy of my credit reports for at least 2 years. **(20 points)**
- I do not believe that people would root around in my trash looking for financial or personal information. **(10 points)**

*Used with permission of the Privacy Rights Clearinghouse

100+ points = You are at high risk. 7-10 million people were victims of ID theft last year.

50-100 points = Your odds of being victimized are about average. 0-50 points = Congratulations you have a high Identity Theft IQ.



Real Estate

Real Estate Withholding Changes Effective January 1, 2007

For sales of California real property on or after January 1, 2007, sellers may now elect to compute the California tax withholding based on their maximum tax rate multiplied by the reportable gain, instead of the standard withholding amount of 3 1/3% of the sales price. Make sure you calculate which number is better for your circumstances. If you elect the alternative withholding amount, you must file Form 593-E with your escrow company. Check for accuracy - the penalty for knowingly executing a false Exemption Certificate is \$1,000 or 20% of the amount required to be withheld. [Source: Spidell's California Taxletter, Vol. 28, No. 11, November 1, 2006]



Reminders And Other Items of Note

Contractors Beware!

Effective January 1, 2007 the Contractors' State License Board is authorized to suspend a contractor's license if the contractor employs an individual in a position requiring a license and that individual has an unpaid tax obligation with the FTB, EDD or the Department of Industrial Relations. However, such persons may serve in non-supervising employee roles. This law can also affect licensed entities with which those persons are associated. The only good news is that the Contractors' State License Board must give the contractor 60 days notice before the suspension. Use this 60 days to either pay the amount due and avoid suspension, or to disassociate from another contractor or entity. [Source: Spidell's California Taxletter, Vol. 28, No. 9, September 1, 2006]



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Dates To Remember

February 2	Groundhog Day
February 4	Super Bowl Sunday
February 12	Lincoln's Birthday—some courts and government offices closed
February 14	Valentine's Day
February 19	Presidents Day - courts and government offices closed
March 17	St. Patrick's Day
April 1	April Fools Day

Did You Know?

- It takes 80 feet of wire to make one slinky.
- Strawberries are the only fruit with the seeds on the outside.
- The longest one syllable word in the English language is "screeched."
- The human brain is 80% water.
- Henry Ford is also the father of the charcoal briquette.
- No words in the English language rhyme with orange, silver or purple.

We appreciate your referrals!



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