

### **Limited Liability Company**

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In effect, an LLC is a limited partnership with no general partner who is personally liable for all activities of the partnership (company).

Tax status is either a partnership or a corporation. Partnership tax status is desirable for:

- 1.Flow through of income.
- 2.Tax free contribution and distribution of property.
- 3.Flexibility to add partners and capital tax free anytime.
- 4.New partners receive stepped up tax basis in share of assets.

Corporate tax status is desirable for:

- 1.Establishing another tax paying unit which may reduce taxes.
- 2.Limiting earned income to reduce social security.
- 3.Establishing more deductible fringe benefits.

An LLC can now elect to be taxed as either a partnership or a corporation on its first tax return.

Under the Michigan LLC statute, membership is limited to the unanimous consent of all members. An LLC is dissolved at the death, withdrawal, expulsion, bankruptcy or dissolution of a member unless: (1) within 90 days a majority of members consent to continue; or (2) continuation is provided for in the operating agreement. Recent legislation now allows a one-member LLC.

The tax basis of a member's interest in an LLC includes:

- 1.Contributions of capital and/or assets.
- 2.Plus earnings less losses over time.
- 3.Plus share of liabilities only if they have been personally guaranteed by the member.

Management can be handled by the members as a group, as in a partnership, or management can be hired as in a corporation.

To operate as an LLC:

- 1.Must set up articles of organization filed with the State to include a registered office and a registered agent (cost \$50).
- 2.Name must include words "Limited Liability Company," or "LLC," or "LC" (approximate cost \$25).

The Limited Liability Partnership is treated tax-wise the same as a partnership. The key characteristic is that no partner is personally liable for the individual acts of another partner. This is desirable for personal service organizations such as accountants, doctors and lawyers.

### Comparison of Business Organizations

	<b>Sole Proprietor</b>	<b>Partnership</b>	<b>Limited Liability Company</b>	<b>Corporation (Sub S)</b>	<b>Corporation (Schedule C)</b>
Nature of entity	Single individual	Aggregate of two or more individuals	A legal person which is an aggregate of two or more members. In some states, including Michigan, a single member is allowed.	Legal person separate from shareholder owners; maximum 75 shareholders who must be individuals or electing Small Business Trust	Legal person separate from shareholder owners; no restrictions on who can be stockholders
Life of business	Terminates on death	Agreed term; terminates at death of a partner	Time specified in agreement or to any transfer of ownership of a member	Perpetual or fixed term of years	Perpetual or fixed term of years
Liability	Personally liable	Each partner liable for all partnership obligations	Member not personally liable for limited liability company's obligations	Shareholders not liable for corporate obligations	Shareholders not liable for corporate obligations
Source of capital	Personal investment; loans	Partners' contributions; loans	Contributions of members; loans	Contributions of shareholders for stock; sale of stock; bonds and other loans	Contributions of shareholders for stock; sale of stock; bonds and other loans
Management decisions	Proprietor	Agreement of partners	Agreement of members; can have a hired manager(s)	Shareholders elect directors who manage business through officers selected by directors	Shareholders elect directors who manage business through officers selected by directors
Limits on business activity	Proprietor's discretion	Partnership agreement	Articles of organization and state corporation law (can be formed to provide professional services)	Articles of incorporation and state corporation law	Articles of incorporation and state corporation law
Transfer of interest	Terminates proprietorship	Dissolves partnership; new partnership may be formed if all agree; new partner receives FMV basis in assets if elected by partnership	Dissolves the limited liability company; remaining members must vote to continue; new member has stepped up basis in assets if elected by company	Transfer of stock does not affect continuity of business--may be transferred to outsiders if no restrictions; no change in basis of assets	Transfer of stock does not affect continuity of business--may be transferred to outsiders if no restrictions; no change in basis of assets
Effect of death	Liquidation	Liquidation, however, the estate can continue as a member, or can sell its interest	Dissolves the limited liability company; remaining members must vote to continue	No effect on corporation; stock passes by will or inheritance; individuals only can be continuing stockholders	No effect on corporation; stock passes through the estate
Income taxes	Income taxed to individual @ individual rates	Partnership files an information return, but pays no tax; each partner reports share of ordinary income or loss, capital gains and losses as an individual; income of a general partner subject to S.E. tax; income of a non-participating limited partner not subject to S.E. tax; withdrawals non-taxable to the extent of basis	Limited liability company files a partnership return; each member reports share of income or loss as an individual; flexible as to allocation of income; income is self-employment income for all participating members; withdrawals non-taxable to the extent of basis	Corporation files an information return, but pays no tax; each shareholder reports share of income, deductions, losses, and credits of the corporation; distributions and allocations must be equal per share; salaries subject to employment taxes; share of income not subject to S.E. tax; withdrawals non-taxable to extent of basis	Corporation files a tax return and pays tax on income; salaries to shareholder-employee's deductible; capital gains offset by capital losses; 15% on the first \$50,000; 25% on the next \$25,000; 34% on the next \$25,000; 39% on the next \$235,000; 34% on all over \$335,000 up to 10 million, then 35% on income up to 15 million; a 3% surcharge then phases out the benefit of the 34%

					bracket; salaries subject to employment taxes; dividends taxable to stockholder
Effect of dissolution	No effect	Property distributed according to share of ownership tax-free	Property distributed according to share of ownership tax-free	Assets distributed to a stockholder must be sold by the corporation	Property distributed must be sold by the corporation; cash distributed is a taxable dividend
Effect of contributions	No effect	Property can be contributed for a partnership interest, tax-free at any	Property can be contributed for a member interest, tax-free at any time	Initial contributions to form the corporation are tax-free; later	Initial contributions to form the corporation are tax-free; later