

# IMMIGRANTS **RISING**

## **CHOOSING A BUSINESS STRUCTURE**

**[immigrantsrising.org](http://immigrantsrising.org)**

# Choosing a Business Structure

One very important step in getting started is determining how to structure your business. You can choose to operate your business as a sole proprietorship, partnership, corporation, or Limited Liability Corporation (LLC), among others.

While the process of incorporation is the same as it is for U.S. citizens and is handled at the state, not federal level, it's important to understand and get advice about the ownership status and tax ramifications of your chosen entity. For example, an S Corporation is very popular among entrepreneurs due to certain tax benefits, but its shares can only be held by U.S. citizens and resident aliens, while an LLC or C Corporation has no restrictions on non-U.S. citizen owners.

## Basic Facts

### Sole Proprietorship

- A sole proprietorship is a type of business entity owned and run by one individual where there is no legal distinction between the owner and the business.
- In most cases, you may use your SSN or ITIN to start a sole proprietorship. Only in certain circumstances, such as hiring an employee, would you have to apply for an [EIN](#) (which you may get using an ITIN).
- With a sole proprietorship, you may use a trade name or a business name other than your own legal name to do business; there is a requirement to file a doing business as (dba) statement with a local government agency, such as the county clerk's office
- Working as a sole proprietor still means that you are working as an independent contractor, so you are held liable for all debts incurred by the business.

### Partnership

- A partnership is the relationship existing between two or more persons who join to carry on a trade or business.
- Similar to a sole proprietorship, each partner may use his or her SSN or ITIN. A partnership may use the surnames of the individual partners or may use a fictitious business name.
- A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax. Instead, it "passes through" any profits or losses to its partners. Each partner includes his or her share of the partnership's income or loss on his or her tax return.

### Corporations

- A corporation conducts business, realizes net income or loss, pays taxes and distributes profits to shareholders.
- Immigrants, regardless of legal status, are able to form C corporations, but not S corporations.
- You must obtain an [EIN](#) to start a corporation (which you may get with an ITIN).

- A corporation is formed under the laws of the state in which it is registered.
- To form a corporation you'll need to establish your business name and register your legal name with your state government.
- Even though employment authorization is not required to form a corporation, there may be additional requirements in the formation process that may require a SSN. Check with a trusted attorney and your local city clerk for specific requirements.
- Although requirements vary across different jurisdictions, C corporations are required to file state, income, payroll, unemployment and disability taxes. Be on the lookout for double taxation.

LLCs/Worker Coops (more detailed information is found on [immigrantsrising.org](http://immigrantsrising.org))

- A Limited Liability Company (LLC) is a business structure allowed by state statute that provides the limited liability features of a corporation and the tax efficiencies and operational flexibility of a partnership.
- Owners of an LLC are called members (not employees). However, if its workers do not have significant ownership and control over the management of the business, they will likely be considered employees.
- Immigrants, regardless of legal status, and even entities based outside of the U.S. may form and own a LLC in the U.S. However, additional information or licenses may be required by your state or local jurisdiction.
- A worker cooperative is a business comprised of members who are both workers and owners of the business. Members can control the structure and practices of the work environment.
- Businesses who hire a worker cooperative are hiring the cooperative not a single member. Therefore, they are not required to prove that the work being done by the worker cooperative qualifies as independent contract work.
- Businesses that hire a LLC are not typically required to obtain any information about the worker-owners of the LLC. In other words, as a worker-owner of a LLC, you should not be required to provide any personal information (your name or even an ITIN) to that business.
- Even though employment authorization is not required to form a LLC, there may be additional requirements in the formation process that may require a SSN. Check with a trusted attorney and your local city clerk for specific requirements.
- Depending on the state that the LLC is established in, there are taxes to be paid. In California a LLC is taxed at the entity level, which means an \$800/ year minimum franchise tax is imposed on every LLC, regardless of gross receipts or net income.

# Sole Proprietorship

Definition: An independent contractor may wish to start his or her own company and provide services in the form of a sole proprietorship. A sole proprietorship is a type of business entity owned and run by one individual where there is no legal distinction between the owner and the business. <sup>1</sup>

Personal information required: In most cases, you will use your SSN or ITIN to start a sole proprietorship. Only in certain circumstances, such as hiring an employee, would you have to apply for an [EIN](#). Similar to independent contractor work, there is no requirement for you to have work authorization. However, you must abide by Federal Statute 8 U. S. Code 1324a(a)(4) <sup>2</sup>, which prohibits an individual or entity from knowingly engaging an unauthorized individual to provide services as a contractor.

With a sole proprietorship, you may use a trade name or a business name other than your own legal name to do business; there is a requirement to file a doing business as (dba) statement with a local government agency, such as the county clerk's office. It's important to note that when you form a business, the legal name of the business defaults to the name of the person or entity that owns the business, unless you choose to rename it and register it as a DBA name.

Liability and taxes: Working as a sole proprietor still means that you are working as an independent contractor, so you are held liable for all debts incurred by the business. You have the same liability, should follow the same guidelines, and must use the same tax forms as an independent contractor. <sup>3</sup>

## Steps to Setting Up a Sole Proprietorship in California <sup>4</sup>

1. Start with a business plan.
2. If you use a business name that is different from your legal name, California requires you to file a Fictitious Business Name Statement in the county recorder's office where the business is located. <sup>5</sup> The cost is about \$35 depending on the type of business.
3. Go to city hall to register the business and get a business license. The cost varies by city, but it is generally around \$10. You may consider asking for a business tax

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<sup>1</sup> For more information about sole proprietorships, visit <https://www.irs.gov/businesses/small-businesses-self-employed/sole-proprietorships>.

<sup>2</sup> United States Code, 2006 Edition, Supplement 5, Title 8 - ALIENS AND NATIONALITY <https://www.gpo.gov/fdsys/granule/USCODE-2011-title8/USCODE-2011-title8-chap12-subchapII-partVIII-sec1324a/content-detail.html>

<sup>3</sup> For more information about taxes you may be liable for and the forms needed for a sole proprietorship, see <https://www.irs.gov/businesses/small-businesses-self-employed/sole-proprietorships>.

<sup>4</sup> For more information about starting a business in CA, see <http://www.sos.ca.gov/business-programs/business-entities/starting-business>

<sup>5</sup> For more information about name availability in CA, see <http://www.sos.ca.gov/business-programs/business-entities/name-availability/>

exemption form, usually provided to first time business owners. [Here](#) is an example of one.

4. Research other licenses or permits needed to conduct your specific business. You may obtain this information by going to the [California Governor's Office of Business and Economic Development CalGold website](#).
5. Open a business account at a bank using a SSN, ITIN or [EIN](#).
6. Other requirements may have to be fulfilled depending on the county, such as registering with the local newspaper.
7. Report and pay taxes using your SSN, ITIN or [EIN](#) (if hiring employees).

## Partnership

Definition: A partnership is the relationship existing between two or more persons who join to carry on a trade or business. Each person contributes money, property, labor or skill, and expects to share in the profits and losses of the business. It is recommended, but not legally mandatory, that both parties draft and sign a partnership agreement. <sup>6</sup>

Personal information required: Similar to a sole proprietorship, each partner may use his or her SSN or ITIN. A partnership may use the surnames of the individual partners or may use a fictitious business name.

Liability and taxes: A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax. Instead, it "passes through" any profits or losses to its partners. Each partner includes his or her share of the partnership's income or loss on his or her tax return. Partners are not employees and should not be issued a Form W-2. The partnership must provide copies of Schedule K-1 (Form 1065) to the partners by the date Form 1065 is required to be filed, including extensions.<sup>7</sup>

## Corporations (S and C)

Definition: In forming a corporation, prospective shareholders exchange money, property, or both, for the corporation's capital stock. A corporation conducts business, realizes net income or loss, pays taxes and distributes profits to shareholders. <sup>8</sup> Immigrants, regardless of legal status, are able to form C corporations, but not S corporation. However, additional information or licenses may be required by your state or local jurisdiction. This section provides a general overview of corporations. We encourage you to research the specific aspects of forming a corporation in your current jurisdiction and seek advice from an attorney familiar with local laws.

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<sup>6</sup> For more information about partnerships, visit <https://www.sba.gov/starting-business/choose-your-business-structure/partnership>.

<sup>7</sup> For more information about taxes you may be liable for and the forms needed for partnerships, see <https://www.irs.gov/businesses/small-businesses-self-employed/partnerships>.

<sup>8</sup> For more information about corporations, visit <https://www.sba.gov/starting-business/choose-your-business-structure/corporation>.

Most corporations are C corporations, which are independent legal entities owned by shareholders. This means that the corporation itself, not the shareholders that own it, is held legally liable for the actions and debts the business incurs. C corporations generally take the same tax deductions as a sole proprietorship to figure its taxable income. A corporation can also take special deductions. For federal income tax purposes, a C corporation is recognized as a separate taxpaying entity.

An S corp is a corporation with the Subchapter S designation from the IRS. What makes the S corp different from a traditional corporation (C corp) is that profits and losses can pass through to your personal tax return. Consequently, the business is not taxed itself, only the shareholders are taxed. There is an important caveat, however: any shareholder who works for the company must pay him or herself "reasonable compensation." Basically, the shareholder must be paid fair market value, or the IRS might reclassify any additional corporate earnings as "wages."<sup>9</sup> Unfortunately, under U.S. tax law, S corporations cannot have a "nonresident alien as a shareholder"<sup>10</sup>, which means that undocumented individuals are not eligible to apply for S corporations or be part of one.

Personal information required: You must obtain an [EIN](#) (discussed [here](#)) to start a corporation. A corporation is formed under the laws of the state in which it is registered. To form a corporation you'll need to establish your business name and register your legal name with your state government. If you choose to operate under a name different than the officially registered name, you'll most likely have to file a DBA. State laws vary, but generally corporations must include a corporate designation (Corporation, Incorporated, Limited) at the end of the business name. Note: even though employment authorization is not required to form a corporation, there may be additional requirements in the formation process that may require a SSN. Check with a trusted attorney and your local city clerk for specific requirements.

Liability: C corporations limit the personal liability of directors, shareholders, employees and officers. Legal obligations of the business cannot become personal debt obligations of any individual associated with the business.

Taxes: Although requirements vary across different jurisdictions, C corporations are required to file state, income, payroll, unemployment and disability taxes. One major downside of C corporations is the double taxation that occurs. After deducting business expenses and salaries, the remaining income is subject to tax. This net income is also distributed to shareholders in the form of dividends. These dividends are income to the shareholder and are reported on the individual's tax return. Therefore, profits from a C corporation are taxed at the corporation's tax rate and individual's tax rate. Only net income retained by the C corporation temporarily avoids double taxation.<sup>11</sup>

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<sup>9</sup> <https://www.sba.gov/starting-business/choose-your-business-structure/s-corporation>

<sup>10</sup> [http://uscode.house.gov/view.xhtml?req=\(title:26%20section:1361%20edition:prelim\)](http://uscode.house.gov/view.xhtml?req=(title:26%20section:1361%20edition:prelim))

<sup>11</sup> For more information about taxes you may be liable for and the forms needed for corporations, see <https://www.irs.gov/businesses/small-businesses-self-employed/corporations>.

## Limited Liability Company (LLC)

A Limited Liability Company (LLC) is a business structure allowed by state statute that provides the limited liability features of a corporation and the tax efficiencies and operational flexibility of a partnership. Owners of an LLC are called members (not employees). However, if its workers do not have significant ownership and control over the management of the business, they will likely be considered employees. Most states do not restrict ownership, so 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. Each state may use different regulations and you should check with your state if you are interested in starting a Limited Liability Company. Immigrants, regardless of legal status, and even entities based outside of the U.S. may form and own a LLC in the U.S. However, additional information or licenses may be required by your state or local jurisdiction. This section provides a general overview of LLCs. We encourage you to research the specific aspects of forming a LLC in your current jurisdiction and seek advice from an attorney familiar with local laws. For more detailed information about LLCs, we encourage you to watch our webinar about Worker Coops and LLCs and download the corresponding guide on our website: [immigrantsrising.org](http://immigrantsrising.org)

### Starting a LLC as a Worker Cooperative

**Definition:** A worker cooperative is a business comprised of members who are both workers and owners of the business. Members can control the structure and practices of the work environment. Businesses who hire a worker cooperative are hiring the cooperative not a single member. Therefore, they are not required to prove that the work being done by the worker cooperative qualifies as independent contract work.<sup>12</sup>

**Personal Information Required:** Businesses that hire a LLC are not typically required to obtain any information about the worker-owners of the LLC. In other words, as a worker-owner of a LLC, you should not be required to provide any personal information (your name or even an ITIN) to that business. Note: even though employment authorization is not required to form a LLC, there may be additional requirements in the formation process that may require a SSN. Check with a trusted attorney and your local city clerk for specific requirements.

**Liability:** A LLC is an unincorporated business organization, whose members are NOT responsible for the debts of the company. Obligation is limited to their investment in the company, and each member of the LLC has the power to make decisions regarding the business.

**Taxes:** Depending on the state that the LLC is established in, there are taxes to be paid. In California a LLC is taxed at the entity level, which means an \$800/ year minimum franchise tax is imposed on every LLC, regardless of gross receipts or net income. Also, every year an

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<sup>12</sup> “Limited Liability Company (LLC),” State of California Franchise Tax Board, [http://www.ftb.ca.gov/businesses/bus\\_structures/LLcompany.shtml](http://www.ftb.ca.gov/businesses/bus_structures/LLcompany.shtml)

FTB Form 568 must be filed and, if the LLC has revenues over \$250,000, it must pay an annual fee based on the total income for the year. <sup>13</sup>

#### Steps to Setting Up a LLC in California <sup>14</sup>

1. The group of workers must research the type of business plan they want and the state regulations.
2. An agreement is made that establishes how the business will be managed, who the members will be, how membership will be granted or revoked, and any other details.
3. To become a LLC in California, a person or group must file Articles of Organization with the Secretary of State along with a fee of \$70. The articles can be filed by filing a form on the Secretary of State's website.
4. The group should develop a management agreement. In California, the Beverly-Killiea Limited Liability Company Act, Corp C 1700-17655 contains rules regarding internal management.
5. Within 90 days of filing the articles, the LLC must file a Statement of Information with the Secretary of State. This includes names and addresses of LLC management and all members of the LLC, the general nature of the LLC's business activities, the name and address of the LLC's agent of service of process and the address of the LLC's principal business office. The statement would be filed every 2 years and when the information changes.
6. The LLC must obtain an Employer Identification Number ([EIN](#)) as its business tax identification number. The process of completing an [EIN](#) application on Form SS-4 can be done online, by phone, or through your attorney.

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<sup>13</sup> For further information on taxes for LLC, see <http://www.irs.gov/businesses/small/article/0,,id=98277,00.html>

<sup>14</sup> "Limited Liability Company (LLC)," State of California Franchise Tax Board, [http://www.ftb.ca.gov/businesses/bus\\_structures/LLcompany.shtml](http://www.ftb.ca.gov/businesses/bus_structures/LLcompany.shtml)

# Pros and Cons for Each Business Structure<sup>15</sup>

TYPE	PROS	CONS
<b>Sole Proprietorships</b>	<ul style="list-style-type: none"> <li>• Easy to set up</li> <li>• Low start-up costs</li> <li>• Net losses can be deducted from personal tax</li> </ul>	<ul style="list-style-type: none"> <li>• As the owner, you are responsible for debts and other liabilities</li> <li>• You pay income taxes on your business's net profits</li> </ul>
<b>General Partnerships</b>	<ul style="list-style-type: none"> <li>• Easy to start up</li> <li>• Low start-up costs</li> <li>• Net business losses can be deducted from owners' personal taxes</li> </ul>	<ul style="list-style-type: none"> <li>• Owners are responsible for debts and other liabilities</li> <li>• Owners pay income taxes on the business's net profits</li> </ul>
<b>Corporations</b>	<ul style="list-style-type: none"> <li>• Owners' responsibility for debts and other liabilities is limited</li> <li>• In certain cases, benefits can be deducted as business expenses</li> <li>• Taxes can be lowered when owners and the business share profits</li> </ul>	<ul style="list-style-type: none"> <li>• Can be more expensive to create than both sole proprietorships and partnerships</li> <li>• Legal paperwork must be filed with your state</li> <li>• The business is a separate tax entity that must pay taxes at the corporation's tax rate and individual's tax rate</li> </ul>
<b>LLC's</b>	<ul style="list-style-type: none"> <li>• Owners' responsibility for debts and other liabilities is limited even if they have control of the business</li> <li>• Profits and losses do not have to be allocated according to ownership interest</li> <li>• Owners get to choose whether the LLC is taxed as a partnership or a corporation</li> </ul>	<ul style="list-style-type: none"> <li>• LLCs are more expensive to establish than partnerships and sole proprietorships</li> <li>• Legal paperwork must be filed with your state</li> <li>• LLCs are taxed at the entity level and a franchise tax may be imposed (varies by state) and pay a revenue fee based on total income for the year</li> </ul>

<sup>15</sup> Modified from <https://www.fundera.com/blog/business-entity>

## About Immigrants Rising

Founded in 2006, Immigrants Rising transforms individuals and fuels broader changes. With resources and support, undocumented young people are able to get an education, pursue careers, and build a brighter future for themselves and their community. Immigrants Rising is a fiscally-sponsored project of Community Initiatives. For more information, visit [www.immigrantsrising.org](http://www.immigrantsrising.org).

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