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Differences Between Corporation and LLC

Corporations and limited liability companies (LLCs) are the most prevalent business forms when foreign investors considering investment in U.S. Both corporations and LLCs have a statutory right to exist perpetually. The shareholders of a corporation and the members of an LLC are not personally liable for the debts, obligations and liabilities of the entity.

However, corporations and LLCs have specific characteristics that must be considered carefully because they may be an advantage to certain investors but not to others.

1. Management

Corporations have mandatory centralized management. Control of the business and affairs of the corporation is vested in the corporation's board of directors, and the shareholders are generally not involved in the day-to-day management of the affairs of the corporation. However, shareholders' approval is required for certain significant transactions such as mergers.

On the other hand, an LLC has a flexible management structure. The LLC can be managed either by the members themselves (member-managed LLC) or by managers (manager-managed LLC) appointed by the members. Any member may act as the LLC's manager. In the manager-managed LLC, the manager is in charge of the company's daily operations.

2. Taxation

A corporation's income may subject to double taxation. A corporation must pay taxes on its income when earned, and the shareholders must pay taxes on any dividends or other distributions they received from the corporation. However, the corporation can choose to retain the earnings to finance growth and reasonable needs of the business up to USD 250,000 (USD 150,000 for personal service corporation) to avoid double taxation. Accumulated Earnings Tax with tax rate 20%, in addition to regular income tax, will be applied on corporations for unreasonably accumulating earnings exceed USD250,000 (USD 150,000 for personal service corporation).

For income tax purpose, a single member LLC is treated as a sole proprietorship, and a multi-member LLC (at least 2 members) is classified as a partnership. Either way, the LLC is taxed as a pass-through entity by default.

As a pass-through entity, an LLC needs to file tax return for the business, but does not pay entity-level taxes on its income; instead, profits and losses pass through to the members, then the members will report the apportioned profits/losses on their own income tax returns with applicable tax rates, regardless of whether the income is distributed or not. If the LLC is profitable but does not distribute any cash to the owners, the owners are still subject to tax on the income of the LLC. If the LLC has a loss, then the owner can take advantage of company losses on their own tax returns.

If you wish to obtain more information or assistance, please visit our official website at www.kaizencpa.com or contact us through the following means:
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