

Entity Classification Optimization (S Corporation)

Making the Right Decision for Your Business



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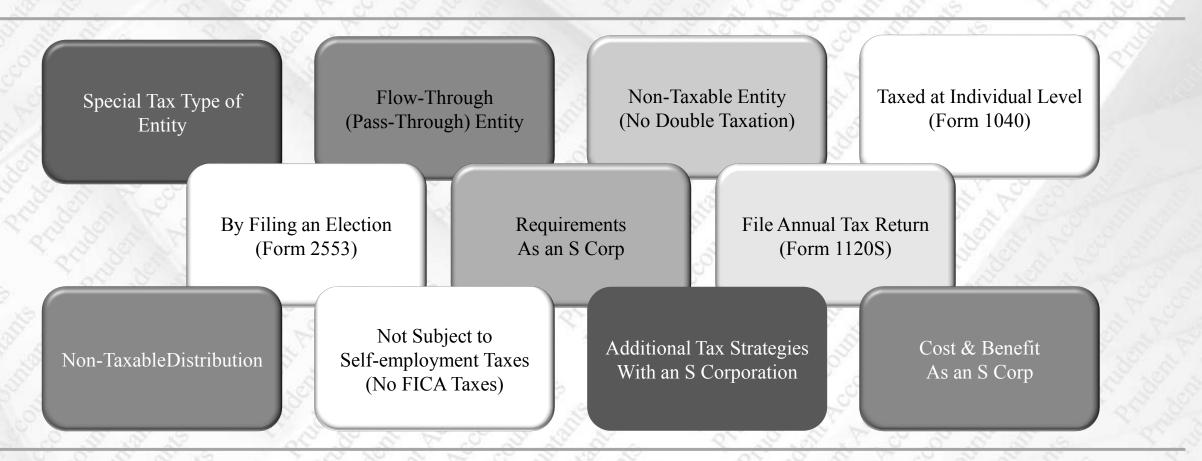
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(1) What Is S Corporation?

An S Corporation is a special tax type of corporation that elect to pass corporate income, losses, deductions, and credits to their shareholders. Accordingly, shareholders of S corporations report the flow-through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates <u>without being subject to self-employment taxes or double taxation at the corporate level.</u>



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(2) Pros & Cons of S Corporation

S Corporation Vs. Schedule C (Sole Proprietorship or Single Member LLC / Disregarded Entity)

Vs. Pros Cons **Separate Business Tax Return** No Self-employment Taxes Not subject to 15.3% of self-employment taxes on net profits Filing Requirement (Form 1120S) **Payroll Processing Requirement** Various Another Tax Strategies Applicable Owners need to process payroll as an employee of S Corp **Limited Liability Protection Financial Statements Requirement** by separating business from personal Balance Sheet / Profit&Loss for Reporting & Basis Tracking **S Corp Basis Limitation Rule Easier Ownership Transfer** & Capital Gain, If Excess Distribution

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(3) Tax Reporting: S Corporation Vs. Schedule C

Example Assumptions,

- Single filer, having \$100,000 of net business income (\$150,000 of gross revenue and \$50,000 of expenses) & no other source of income
- Take 60% of net income from business for personal use & reinvest 40% to future business or the market value of service provided by owner is \$55,000 based on the state average hourly rate jobs category

S CORPORATION SCHEDULE C Pass Through Form 1040 Form 1040 Form 1120-S Taxable Wage(W-2): \$55,000 Taxable Wage(W-2): Gross Income: Income from S Corporation: \$37,935 Self-employment Income: \$100,000 (-) Expenses: (-) Self-employment tax : (-) Self-employment tax: (-) Officer's Salary & Wage: (\$ 55,000)**G** \$92,935 **Adjusted Gross Income: Adjusted Gross Income:** \$ 92,935 (-) Payroll Tax & Fees **Net Income from S Corp:** (Standard & OBI Deduction): (Standard & OBI Deduction): **Taxable Income:** Taxable Income: \$70,748 \$ 62,668 Two Different Type of Cash Flow Income Tax: \$10.613 Income Tax: \$ 8.842 Salary as an Employee of S Corp & Self-employment taxes: Self-employment taxes: \$ 14,129 Distribution as an Owner of S Corp **Total Federal Income Tax: Total Federal Income Tax:** \$10,613 \$ 22,971

\$12,358 of Gross Benefit

(The net benefit will be lower considering compliance costs and payroll taxes.)

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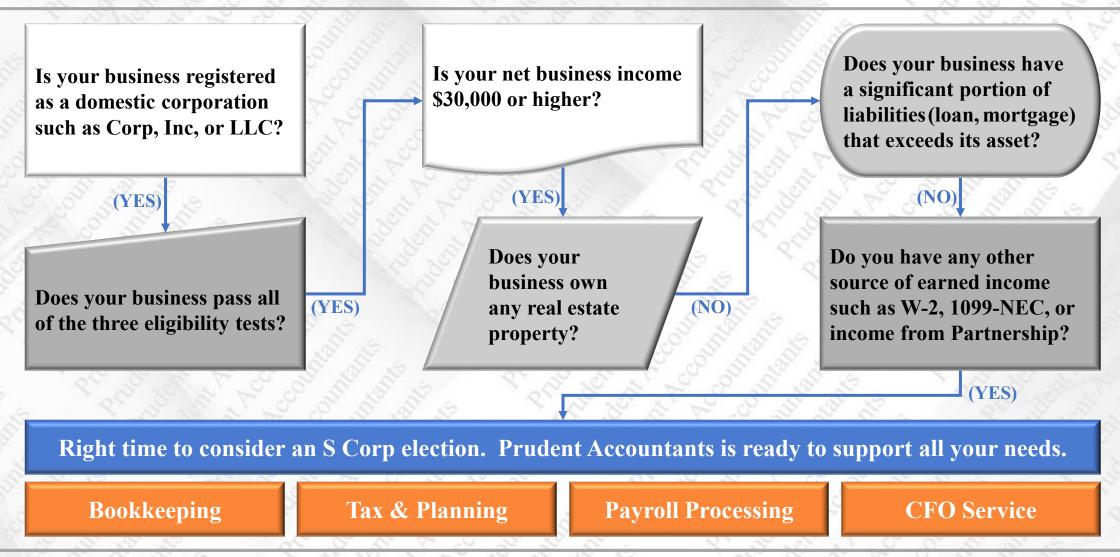
(4) Requirements to Be Eligible for S Corporation

ELIGIBLE (O)	INELIGIBLE (X)
 Domestic Corporation (Inc, Corp, LLC) Having No More than 100 Shareholders 	 Foreign Corporation, Corp Having More than 100 Shareholders Certain Corps(Financial Institutions, Insurance Companies, etc.)
(AND)	(OR)
 Individual (U.S. Citizen & Resident Alien) Certain S Corporation (QSSS) Certain Trusts and Estates 	PartnershipC CorporationNon-Resident Alien
(AND)	(OR)
Have Only One Class of Stock (Proportionate Distribution)	Have Multi Classes of Stocks (Disproportionate Distribution)
	 Domestic Corporation (Inc, Corp, LLC) Having No More than 100 Shareholders (AND) Individual (U.S. Citizen & Resident Alien) Certain S Corporation (QSSS) Certain Trusts and Estates (AND) Have Only One Class of Stock

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(5) Is S Corporation Election Right for My Business?



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