

Do you Really Understand the LLC you Just Established?

Now that you have an LLC, it's Time to make Tax Decisions

By Eva Rosenberg, EA



Living in California, it took me a really long time to gain any understanding of LLCs. I just couldn't figure out why anyone would be foolish enough to set up one of those entities – because California makes them excessively expensive.

Costly in California

In addition to the annual \$800 minimum fee for LLCs, corporations and limited partnerships, the State of California also tacks on a Gross Receipts tax. That means, your LLC pays an extra tax on its sales or receipts BEFORE deducting any expenses. So you could have a million-dollar loss, and still pay an extra \$6,000 in state taxes because your LLC had [gross receipts](#) of \$1,000,000 - \$4,999,999.

Considering this, you can understand my resistance to California LLCs. However, traveling the country, teaching tax professionals, I learned more about how useful they could be in other states...and

even a few reasons they might work in California. Most other states charge far less for their LLCs. To learn more about tax considerations in your own state, visit the Wolters Kluwers resource on [Understanding State Corporate Taxes](#) and [state tax guides](#).

In order to use an LLC, you need to make some choices.

An LLC is filed as?

Having set up your LLC with BizFilings.com is just the beginning of your adventure in business ownership. Now, you have to make a decision on how to report the earnings and activities of that LLC for tax purposes. It's important to make this decision early, because you'll need the information for bank signature cards and before you set up payrolls, sales tax arrangements, and other licensing.



Ignore the Decision – Your Default is...

In its basic form, if you don't make any tax choices, when you set up an LLC you are considered a disregarded entity by IRS. What does that mean?

If one person owns the LLC, you will report all the income and expenses on your own [Schedule C](#) - Profit or Loss From Business or [Schedule F](#) – Farm Income. Or if the LLC owns rental real estate, report all the activity on page 1 of the [Schedule E](#) of your personal tax return.

When two or more people own the LLC, the default entity is a partnership, which files [Form 1065](#).

Those Who Are Clued In

While the disregarded entity may be the easiest option, smart business owners do some planning. You can take advantage of a variety of tax benefits, succession planning, or perhaps lay the groundwork to go public. To make the decision, please talk to your advisory team – your attorney and a smart, [experienced tax professional](#). This is critical if you want to pay the least amount of taxes – and get the most benefits, legally.

An LLC doesn't have to be a humble disregarded entity. It could be powerful and exciting. You can decide to file as an S corporation or C corporation.

To tell IRS you want to file as a corporation, use [Form 8832](#). To tell IRS you want to be an S corporation, use [Form 2553](#). Typically, you need to submit these forms by the 15th day of the 3rd month after you set up the LLC. If you haven't done that yet, don't worry. As long as you file your elections with IRS by the time you file your first tax return, IRS will accept your entity selection.

Once you make your choices, the decision is not set in stone. You can change your entity choice once every 5 years. And if you never made a choice, but have been floating along, filing as a disregarded entity, you can make your first election this year.

LLC Structure Options:

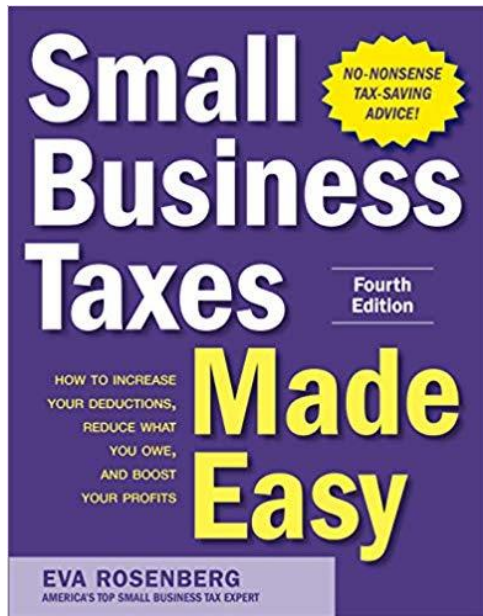
One owner

- Schedule C, Schedule F, Schedule E (Disregarded Entity)
- S Corp
- C Corp

More than one owner

- Partnership (Disregarded entity)
- S Corp
- C Corp

More Resources



Before you leave, please learn a little more. My award-winning book, [Small Business Taxes Made Easy](#), contains a detailed overview of the various business entities – and which could be most beneficial for your business. If you're ready to learn even more about business taxes, sign up our business course for tax professionals – [TaxMama's® EA Course for all Business Entities](#). It's taught so that anyone can learn and understand the concepts.

Eva Rosenberg, EA is the publisher of [TaxMama.com](#) , where your tax questions are answered for free. Eva is the author of several [books and ebooks](#), including [Small Business Taxes Made Easy](#). Eva teaches tax courses at [IRSExams.school](#) and [CPELINK](#).