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Entity selection

Choosing the Right Entity is Crucial for Startup Success

DEFINITION

Entity selection refers to the process of choosing the legal structure for a business. This decision impacts liability, taxes, and operational flexibility.

KEY CONCEPTS

Sole Proprietorship

A business owned by one person, offering simplicity but exposing personal assets to liability.

Partnership

A business structure where two or more individuals share ownership and responsibilities, with shared liabilities.

Limited Liability Company (LLC)

A hybrid entity that combines the benefits of a corporation and a partnership, protecting personal assets.

Corporation

A legal entity separate from its owners, providing limited liability but requiring more regulations and taxes.

Nonprofit Organization

An entity formed for charitable purposes, often exempt from certain taxes and focused on public benefit.

EXAMPLES

- A freelance graphic designer operates as a sole proprietorship for simplicity.
- Two friends start a bakery as a partnership to share costs and responsibilities.
- A tech startup forms an LLC to protect personal assets while enjoying tax benefits.

MEMORY TIPS

- ★ Remember 'Sole' for one owner, 'Part' for shared ownership, 'LLC' for limited liability.
- ★ Think of 'Corp' as a separate body, like a corporation being its own person.
- ★ Use 'Nonprofit' to recall that it focuses on profit for the public good.

COMMON MISTAKES

- ✗ Confusing LLCs with corporations regarding liability and tax implications.
- ✗ Overlooking the importance of state-specific regulations in entity selection.
- ✗ Failing to consider future growth and funding needs when choosing an entity.

QUICK RECAP

Entity selection is vital for startups as it affects liability, taxes, and operations. Understanding the differences between structures like sole proprietorships, partnerships, LLCs, and corporations helps in making informed decisions.