

Law You Can Use: Know legal consequences before forming a business in Ohio

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So, you have a new business idea and you are excited to set up shop and make it big. Before you start selling your product and service, be sure to stop and think about the legal consequences of your business formation. This is a crucial step in creating a successful business in Ohio.

Q: Should I incorporate?

A: Absolutely. Forming either a corporation or an LLC allows you to protect your personal assets in case of a lawsuit or claims against your business. You will also be able to limit your liability for any outstanding business debts and obligations. When starting a business, be sure not to put your personal assets at risk. In the event you are ever sued and you have not incorporated, your home, bank account, and all other assets can potentially be exposed should you receive a court judgment against your business. By incorporating your business, you create a wall between the business assets and your own personal assets. Another benefit of incorporating is that it makes your business more credible to consumers. Just seeing “Inc.” or “LLC” behind your business name adds instant legitimacy. Further, incorporating protects your brand and business name. Finally, incorporation gives your business flexibility and tax benefits.

Q: I’m thinking about going into business with a friend. What should I consider?

A: Depending on the corporate formation you choose, you could very well be liable for your own debts and actions in addition to those of your business partner, over whom you have no control. Think long and hard before committing yourself to such a situation. To help alleviate personal risk in a partnership setting, consider speaking with an attorney or other professional with business start-up expertise who can walk you through this complicated situation and consider options such as placing assets in trust or in another’s name.

Q: A friend told me I should set up an LLC. How do I know if that’s the best choice for me?

A: A limited liability company is the most popular business entity. Like a corporation, an LLC limits your liability, but is treated, for tax purposes, like a partnership. Consult with an attorney, however, before deciding whether an LLC is the best option for you.

Q: What are the differences between an S-Corporation and a C-Corporation?

A: A C-Corporation is legal entity separate and distinct from its owners. The corporation issues ownership interests (“shares”) to “shareholders.” The shareholders elect the board of directors. The directors, who are entrusted with managing the corporation, elect the officers. The officers operate the corporation under the board’s direction. The shareholders, the directors and the officers are generally not responsible for the debts and obligations of the corporation. The corporation’s profits are distributed to the shareholders in the form of dividends.

A C-corporation is taxed twice: first, at the corporate level, when income is received, and second, when income is re-distributed to shareholders. Finally, a person who is merely a shareholder of the corporation will almost always be absolved of liability.

An S-Corporation is similar to a C-Corporation, but it is taxed as a “pass-through entity” meaning that the owners pay taxes on all business profits on their individual tax returns (i.e., the business income “passes through” the business to the owners’ personal tax returns and business profits are not “double taxed”). To become an S-Corporation, a business must have fewer than 100 shareholders, all shareholders must be people (no estates, trusts, etc.) who are not nonresident aliens, and the corporation can have only one class of stock.

Q: How do I create a legal business in Ohio?

A: Surprisingly, it is very easy to set up a corporation, LLC, or other business formation. You simply have to complete a small amount of written paperwork and pay a filing fee. You can get the necessary papers through the Ohio Secretary of State website at www.sos.state.oh.us/sos/upload/business/filingformsfeeschedule.aspx?page=251. You may also draft an operating agreement or other document depending on the business form you choose. For instance, to create a legally binding LLC, you merely have to submit a two-page online Articles of Organization and send the Secretary of State a check for \$99. This is a very small price to pay to avoid personal liability for your business’ debts and actions. You may wish to consult with an attorney to help you choose a business entity and draft an operating agreement.

This “Law You Can Use” column was provided by the Ohio State Bar Association. It was prepared by Andrew L. Smith, a senior associate attorney in the Cincinnati office of Smith, Rolfes & Skavdahl Company, LPA. Articles appearing in this column are intended to provide broad, general information about the law. Before applying this information to a specific legal problem, readers are urged to seek advice from an attorney.