

# Basic Tax Issues in Choosing a Business Entity

April 01, 2015

## BACKGROUND

Businesses can be operated through a variety of entities or through no legal entity at all. An individual who operates a business as a sole proprietorship without forming an entity will be directly taxable on the business income and gain, and may, subject to certain limitations, be able to offset other income and gain with the loss and deduction from the business. The individual reports the sole proprietorship's income, gain, loss and deduction on his or her federal and state tax returns. Two or more individuals who operate a business without forming an entity will nevertheless be taxed as a partnership. Partnerships themselves are not subject to income tax (though they are required to file an income tax return.) Rather, income, gain, deductions and loss generated by the partnership are reported by each partner on his or her federal and state tax returns as allocated by the partners.

Most entrepreneurs, however, choose to operate through a legal entity such as a corporation or a limited liability company ("LLC")<sup>1</sup> for business reasons, including the limitation of liability. Operating through an entity can also facilitate changes in ownership and investments by others. While there are numerous non-tax factors to consider when choosing which form of entity to use, there are also many tax considerations. For example, for tax purposes, corporations may be classified as C corporations or S corporations. C corporations are separate taxable entities for federal and state income tax purposes. A C corporation pays an entity-level tax on its income and gain and only the C corporation may take advantage of any loss and deduction it generates. A C corporation's owners (shareholders) pay another tax on the corporation's distribution of corporate earnings and profits when distributed as a dividend. Unlike a C corporation, an S corporation is not a separate taxable entity for most federal and state income tax purposes. The S corporation's owners (shareholders) pay tax on a proportionate share of the income and gain realized by the company (whether or not it is distributed to them) and may, subject to certain limitations, use the entity's losses to offset other income. There is no tax upon the distribution. Not every corporation, however, is eligible to be an S corporation.

An LLC is like an S corporation in that it is not a separately taxable entity for most federal and state income tax purposes. If an LLC has only one member it is generally taxed like a sole proprietorship. If it has more than one member it is generally taxed under the rules applicable to partnerships. The owners (members) of a multi-member LLC are taxed on their allocable share of the company's income and gain (whether or not it is distributed to them) and may, subject to certain limitations, use the entity's losses to offset other income. As with S corporations, the owners are not taxed when the previously taxed income and gain is later distributed.

While overall income tax burden on a business is an important factor, there are other important non-tax differences between C corporations, S corporations and LLCs. While some of the tax considerations described in this article may tip the balance when choosing an entity under particular facts and circumstances, it is difficult to know exactly which form will result in the lowest overall tax burden. It is possible, however, to be aware of the major tax differences to avoid surprises and prepare accordingly. This article summarizes some of these differences in three broad categories:

- Initial Considerations
- Operational Considerations

- Exit Considerations

Other business entities include limited partnerships, business trusts and specialized entities such as real estate investment trusts (REITS) and real estate mortgage investment conduits (REMICs). These are not addressed in this article.

## INITIAL CONSIDERATIONS

### Income Taxation

As a general rule, C corporations are taxed twice on business income; once when earned by the corporation and again when that income is distributed as a dividend to the shareholders. Income and gains earned by flow-through entities, like S corporations and LLCs, are generally taxed only once – to the owners when earned.

**C corporation** – Two levels of tax – at entity and shareholder levels. Certain high income shareholders may be subject to NIIT on dividends.<sup>2</sup>

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**S corporation** – Tax at shareholder level only, except a former C corporation which distributes C corporation earnings and profits (“E&P”), sells built-in gain property (within 10 years of S election), or has C corporation E&P and excess net passive income. Some states do not recognize the federal S election or may impose a special entity-level tax on S corporations. For example, Massachusetts imposes an entity-level tax on large S corporations.<sup>3</sup> NIIT may apply to certain investments.

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**LLC** – Tax at member level only. Default tax status for a single member LLC is a disregarded entity; default tax status for a multi-member LLC is a partnership. State tax treatment varies. Massachusetts follows the federal classification.

### Qualification Requirements

As a general rule, any person or entity can be a shareholder of a C corporation. S corporation status is available only for certain types of businesses and owners. Certain types of investors (including most VCs), while permitted to be LLC owners, may be reluctant to invest directly in an LLC taxed as a partnership without additional tax planning.

**C corporation** – No restrictions as to owners or type of businesses.

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**S corporation** – Must be a domestic corporation. In addition, certain corporations, such as certain financial institutions, insurance companies, and domestic international sales corporations, are ineligible to be S corporations.

Must make an election on Form 2553 with the consent of all the shareholders before the 16th day of the third month of the taxable year. Example: a corporation which begins its taxable year on January 1 must make the election during the period that begins January 1 and ends before March 16.

Can have up to 100 shareholders. Spouses (and their estates) and all members of a family (and their estates) may be treated as one shareholder.

Shareholders may not be C corporations, nonresident aliens, or partnerships. US citizens resident aliens and estates may be owners. Certain trusts and exempt organizations may be owners.

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Only one class of stock is allowed, but differences in voting rights are permitted.

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**LLC** – None. However, foreign and tax-exempt investors may be reluctant to be members of an LLC due to concerns about U.S. effectively connected income (ECI) and unrelated business taxable income (UBTI). Some VCs are also reluctant to invest directly in LLCs.

#### Taxable Year

Tax advantages may be available by using a fiscal year, i.e. a taxable year that differs from the calendar year. Use of a fiscal year by S corporations and most LLCs taxed as partnerships is limited. The choice of a fiscal year may provide the benefit of deferral of income.

**C corporation** – May adopt either a calendar year or a fiscal year.

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**S corporation** – Must adopt the calendar year, unless the S corporation establishes a business purpose for adopting a fiscal year.

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**LLC** – Generally, must adopt the taxable year of those members holding a majority in interest of profits and capital, unless the LLC establishes a business purpose for adopting a different fiscal year.

#### Method of Accounting

As with the ability to choose a fiscal year, the ability to choose a method of accounting may be tax advantageous. The ability to utilize the cash method of accounting may provide the benefit of deferral of income.

**C corporation** – Accrual method generally required, unless the corporation is a qualified personal service corporation or has gross receipts of no more than \$5 million. Other restrictions, such as those pertaining to inventories, may apply.

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**S corporation** – Cash method or accrual method permitted. Accrual method required if S corporation is a tax shelter. Other restrictions, such as those pertaining to inventories, may apply. An S election by a cash method corporation will trigger built-in gains tax on the realization of cash basis accounts receivable.

**LLC** – Accrual method required if a tax shelter or if a C corporation is a member, unless the C corporation-member is a qualified personal service corporation or LLC has gross receipts of no more than \$5 million.

#### Federal Income Tax Rates

All income of a C corporation, whether ordinary or capital gain, is taxed at the federal corporate rate (up to 35%). Individual owners of S corporations and LLCs may be able to take advantage of the current discrepancy between federal tax rates on an individual's ordinary income and capital gains (39.6% vs. 20%).

**C corporation** – Corporations are taxed at up to 35% on ordinary income and capital gains. Shareholders taxed at 20% on certain dividend distributions.

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**S corporation** – Shareholders who are individuals are taxed at up to 39.6% on ordinary income and 20% on capital gains upon sale of certain property held for more than one year.

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**LLC** – Members who are individuals are taxed at up to 39.6% on ordinary income and 20% on capital gains upon sale of certain property held for more than one year.

#### Tax Basis in Ownership Interest

An owner's tax basis in his or her equity is important for tax purposes because it affects the amount of his or her gain on a sale of the equity, and for an owner of a flow-through entity, his or her tax on distributions and use of flow-through loss. Unlike a shareholder in a C corporation, an LLC owner and an S corporation owner (though to a more limited extent) may include certain business debt in his or her basis.

**C corporation** – Shareholder's basis in his or her stock equals amount of cash and basis of property transferred to corporation less liabilities assumed by the corporation.

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**S corporation** – Shareholder's initial basis in his or her stock equals the amount of cash and the basis of property transferred to corporation less liabilities assumed by corporation. Shareholder's share of company debt is not included in basis, unless the shareholder is the creditor. Basis is increased by cash and basis of additional property contributed and by income allocations and decreased by allocations of losses and by distributions.

**LLC** – Member's initial basis in his or her LLC interest equals the amount of cash and the basis of property transferred to LLC less liabilities assumed by the LLC. Unlike in an S corporation, the LLC member's basis includes his or her share of LLC debt. A member receives no basis for the contribution of a promissory note until payments on the note are made. Basis is increased by cash and the basis of additional property contributed and by income allocations; and decreased by allocations of losses and by distributions.

#### Contribution of Property

The formation of a corporation or LLC by the contribution of property is typically a tax-deferred transaction. However, the rules applicable to an LLC are more favorable, particularly as related to subsequent contributions of property.

**C corporation** – If property is contributed to a C corporation solely in exchange for stock in a transaction in which the contributing shareholders are in control (at least 80% of vote and value) immediately after the transaction, no gain or loss will be recognized. However, a shareholder will be taxable to the extent of "boot" received (including, for example, cash and certain types of stock). Gain may also be triggered to the extent that property is contributed subject to liabilities in excess of the basis of the contributed property. Caveat: gain may also result if the corporation is considered an "investment company."

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**S corporation** – Same as C corporation.

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**LLC** – No gain or loss is recognized upon the contribution of property to an LLC, regardless of amount of control contributing members have immediately after contribution. However, liability shifts can give rise to taxable gain. Careful attention must be given to the contribution of

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encumbered property to an LLC. In addition, payment made to a contributing partner in connection with a contribution of property can cause the contribution to be treated as a partial taxable sale. Caveat: similar to a corporation, gain may result if the LLC would be considered an “investment company.”

### Contribution of Services

The receipt of equity in connection with the performance of services contributed to an entity typically triggers compensation income taxable to the service provider, irrespective of the form of entity. However, services may be contributed to an LLC taxed as a partnership in exchange for a “profits interest” representing only future value without triggering a current tax to the service provider.

**C corporation** – Stock issued in connection with the performance of services will give rise to ordinary income when the stock vests or upon grant pursuant to the making of a Section 83(b) election.

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**S corporation** – Same as C corporation.

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**LLC** – A “capital interest” issued in exchange for the performance of services will give rise to ordinary income when the interest vests or upon grant pursuant to the making of a Section 83(b) election. LLCs can issue “profits interests” which have a zero value upon grant and, thus, do not give rise to additional income. However, a “protective” Section 83(b) election should be considered in the case of an unvested “profits interest.”

### **OPERATIONAL CONSIDERATIONS**

#### Equity Incentives

Only corporations can issue qualified incentive stock options (ISOs). Both corporations and LLCs can issue non-qualified compensatory options (NQOs) and restricted equity. Limitations on the eligibility of S corporation shareholders must be considered. In addition, the tax treatment of issuing NQOs by LLCs taxed as a partnership is uncertain, and are generally not recommended. LLCs can, however, issue “profits interests” to service providers. All entities may also grant awards under equity-like arrangements, such as phantom stock and equity appreciation plans. Rules under Section 409A should also be considered.

**C corporation** – ISOs, NQOs, restricted stock, phantom stock and stock appreciation rights and equity-flavored bonus plans available.

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**S corporation** – Same as C corporation. Caveat: equity incentives must not create a second class of stock, result in a number of shareholders in excess of 100 nor permit ineligible shareholders to own an interest in the S corporation.

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**LLC** – ISOs not available. Caveat: awaiting IRS guidance on LLC NQO tax treatment. Capital interests and profits interests also available. Equity-flavored bonus appreciation plans available.

#### Losses

The ability of owners to use tax losses generated in a business entity against unrelated income and gain can be desirable. While there are significant restrictions on their use, tax losses

generated in an S corporation or LLC may be available for use by its owners. Losses in a C corporation are not available for use by its owners.

**C corporation** – Losses can only be used to offset the C corporation’s own income. Net operating losses, in general, may be carried back 2 years and carried forward 20 years. Capital losses may be carried back 3 years and carried forward 5 years by the corporation to offset income earned in those years.

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**S corporation** – Shareholders may use their pro rata share of losses against their other income, but basis, at risk, and passive loss limitations apply. Shareholders are considered “at risk” for personal loans to the corporation, but not for personal guarantees of corporation debt. Under the passive activity rules, an activity is a passive activity if the shareholder does not materially participate in management. Shareholders who are individuals may carry capital losses forward indefinitely but not back. Shareholders who are individuals may carry ordinary losses back 2 years and forward 20 years.

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**LLC** – Members may use their allocable share of losses against their other income, but basis, at risk, and passive loss limitations apply. Under the passive activity rules, an activity is a passive activity if the member does not materially participate in management. Members are considered at risk for personal loans to the LLC and personal guarantees of LLC debt. Members who are individuals may carry capital losses forward indefinitely but not back. Members who are individuals may carry ordinary losses back 2 years and forward 20 years.

#### Distributions of Cash

Distributions of earnings by a C corporation to its shareholders are generally taxable. Distributions of earnings by a flow-through to its owners are typically not taxable.

**C corporation** – Distributions of cash are generally taxable as dividends to the extent that the distributing corporation has current or accumulated earnings and profits. Distributions beyond current or accumulated earnings and profits are a non-taxable return of capital to the extent of basis and gain from the sale or exchange of property thereafter. Certain high income shareholders may be subject to NIIT on dividends.<sup>4</sup>

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**S corporation** – An S corporation that has no C corporation earnings and profits can distribute cash to a shareholder tax-free to the extent that the cash distributed does not exceed the shareholder’s basis in the stock. Distributions in excess of basis are treated as taxable gain from the sale or exchange of property and may be subject to NIIT to the extent not attributable to an active trade or business. If an S corporation has accumulated earnings and profits, distributions that do not exceed the corporation’s accumulated adjustment account will be tax free. Any distribution in excess of the accumulated adjustment account is taxed as a dividend to the extent of the C corporation earnings and profits.

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**LLC** – Subject to rules regarding “disguised sales,” an LLC can distribute cash to a member tax-free to the extent that the cash distributed does not exceed the member’s basis in its interest. Distributions in excess of basis are treated as taxable gain from the sale or exchange of property and may be subject to NIIT to the extent not attributable to an active trade or business. Under certain circumstances, the distribution of “marketable securities” is treated as the distribution of cash.

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### Distribution of Appreciated Property

The distribution of appreciated property by a corporation can trigger a tax to both the distributing corporation and the recipient shareholder. Most distributions of appreciated property by an LLC taxed as a partnership are not taxable. Thus, if distributions of appreciated property are anticipated, an LLC may be preferable.

**C corporation** – Distribution of appreciated property can result in two levels of tax. Generally, the distributing corporation recognizes gain equal to the difference between the fair market value of the property distributed and the property's adjusted basis. In addition, the distributee shareholder is treated as having received a dividend to the extent of the corporation's earnings and profits.

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**S corporation** – Distribution of appreciated property will generally trigger gain equal to the difference between the fair market value of the property distributed and the property's adjusted basis, which will flow through to the shareholders. Distribution may also be taxable to the recipient shareholder if the value of the property distributed exceeds the shareholder's basis.

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**LLC** – Generally, the distribution of appreciated property to members will not trigger gain or loss to either the distributee member or the LLC.

### Social Security Taxes

Social Security taxes on compensation for services include a 12.4% Social Security component (applies to compensation up to \$118,500 in 2015) and a 2.9% Medicare component (no limit). A 0.9% Additional Medicare component may also apply if a taxpayer's earned income meets certain threshold amounts. In the corporate context, Social Security taxes imposed on all employees are "employment taxes." In the LLC context, Social Security taxes on the compensation of employees who are not owners of the LLC are also "employment taxes"; Social Security taxes on employee-owners of LLCs are "self-employment taxes."

**C corporation** – All employees (whether or not an owner) of C corporations are subject to employment taxes on compensation for services. One half of both the Social Security component and Medicare component is paid by the C corporation from its own funds. The C corporation gets a deduction for the portion of Social Security taxes it pays from its own funds. The other half is paid by withholdings from employee wages. The Additional Medicare component, where it applies, is paid wholly by withholdings from the employee's wages.

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**S corporation** – Same as C corporation. Distributions other than the wages to owners of S corporations who are employees are not subject to employment tax. Careful planning can help to minimize employment tax due on amounts earned by a participating owner in an S corporation. However, the IRS may reclassify distributions as wages, if wages are not "reasonable" in amount.

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**LLC** – An owner who participates actively in the LLC business is subject to self-employment tax on "guaranteed payments" and may be subject to self-employment taxes on the member's entire allocable share of the LLC's business income (other than income such as rents, interest, capital gains, etc.). A taxpayer may deduct half of the self-employment taxes paid in figuring individual adjusted gross income.

### Fringe Benefits for Owner-Employees

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Owner-employees of C corporations may receive a wide array of fringe benefits tax-free from the corporation. Whereas, “2% owners” of S corporations and all LLC members must include the value of fringe benefits provided by the entity in income, but may be eligible to claim an “above the line” deduction.

**C corporation** – Owners of C corporations can receive tax-free a greater range of fringe benefits, such as health insurance, cafeteria plans benefits, and qualified pension plans.

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**S corporation** – “2% owners” of S corporations include the value of fringe benefits in income and may be eligible for an “above the line” deduction.<sup>5</sup>

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**LLC** – LLC owners include the value of fringe benefits in income and may be eligible for an “above the line” deduction.

#### Local Property Taxes

Local property taxes in a particular jurisdiction may not apply in the same manner to C corporations, S corporations and LLCs. For example, in certain jurisdictions, corporations may be eligible for exemptions for which LLCs are not eligible.

**C corporation** – Generally, not subject to local property taxes.

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**S corporation** – May be eligible for local property tax exemptions that are not available to LLCs. These exemptions may be particularly important if the business will have significant amounts of inventory, machinery or other personal property.

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**LLC** – Generally, subject to local property taxes.

#### Treaty

**C corporation** – A corporation is generally entitled to the benefits of a treaty between the U.S. and another country.

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**S corporation** – As a flow-through entity, the S corporation itself will not be entitled to treaty benefits, rather treaty benefits may be claimed by owners who themselves qualify for benefits under the treaty. Caution: if a dual resident taxpayer claims a treaty benefit as a non-resident alien for U.S. tax purposes, he or she may not be treated as an eligible S corporation shareholder.

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**LLC** – As a flow-through entity, the LLC itself will not be entitled to treaty benefits, rather treaty benefits may be claimed by owners who themselves qualify for benefits under the treaty.

### **EXIT CONSIDERATIONS**

#### Liquidation

As with distributions of appreciated property, liquidation by a corporation can trigger taxable gain. Most liquidations by an LLC are not taxable. Thus, if a liquidation is anticipated, an LLC may be preferable.

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**C corporation** – Tax at the corporate level on appreciated property distribution and tax at the share holder level on capital gain and NIIT on certain high income shareholders.

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**S corporation** – Shareholder taxable on appreciation in value of S corporation property distributed. Taxable also on distribution in excess of basis as capital gain. NIIT on certain high income shareholders.

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**LLC** – Nontaxable generally, unless money and/or marketable securities distributed are in excess of adjusted basis of membership interest or unless member is relieved of debt in excess of adjusted basis.

#### Changes in Form

Changing form from a corporation to an LLC can present significant tax challenges. Starting out as an LLC may be the right choice if it is unclear that one form is more advantageous in the short or long-term.

**C corporation** – A C corporation that makes an S corporation election, may be subject to LIFO recapture. Additional tax on built-in gains and excess passive income may also apply. Changing entity form from a C corporation to an LLC, whether by merger or state law conversion, is taxable.

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**S corporation** – Loss of S corporation status (whether voluntarily or involuntarily) which results in the S corporation being taxed as a C corporation will generally not trigger tax consequences. A change in form from an S corporation to an LLC is taxable.

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**LLC** – Generally, an LLC may change its form to either C corporation or S corporation status without triggering gain unless a member is relieved of debt in excess of this basis.

#### Tax-Free Reorganizations

Tax-free reorganizations are only available for C corporations and S corporations. Only with advance planning can an LLC (which must change to a corporation) take advantage of the tax-free reorganization rules.

**C corporation** – Tax-free reorganization provisions apply.

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**S corporation** – Tax-free reorganization provisions apply.

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**LLC** – Tax-free reorganization provisions do not apply; however, with proper advance planning, may be able to change to corporate status and take advantage of tax-free reorganization provisions.

#### Taxable Sale of Substantially All Assets

One level of tax upon a taxable asset sale provides an advantage to S corporation and LLC forms of business. Be aware, however, in certain situations, the taxable sale of S corporation assets

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may trigger a second level of tax as described below. One level of taxation might also be available to the corporate parent in connection with the sale of the assets of an 80% owned corporate subsidiary.

**C corporation** – A C corporation will recognize gain or loss on a taxable sale of its assets. The character of the gain (ordinary or capital) depends on the nature of the assets. If a liquidating distribution is made, shareholders will also recognize gain or loss (unless the shareholder is a corporate shareholder that owns at least 80% of the voting power and value of the liquidating corporation). Gain from a sale is generally eligible for the installment method, except for gain from the sale of inventory, cash basis receivables and recapture income, which must be reported immediately.

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**S corporation** – Gain or loss realized by an S corporation on the taxable sale of its assets is passed through to shareholders. The character of the gain (ordinary or capital) depends on the nature of the asset sold. The gain increases the shareholders' stock bases so that distribution of sale proceeds is generally not subject to a second level of tax. There is potential for an entity-level tax if the built-in gains tax applies or, if taxable in a state such as Massachusetts that imposes a "sting tax" on S corporations. Gain from a sale is generally eligible for the installment method, except for gain from the sale of inventory, cash basis receivables, and recapture income, which must be reported immediately.

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**LLC** – Gain or loss realized by an LLC on the taxable sale of assets is passed through to the members. The character of the gain (ordinary or capital) depends on the nature of the asset sold. The gain increases the members' bases in their interests so that distribution of sale proceeds is not subject to a second level of tax. Caveat: gain may be recognized if losses generated by distribution have been allocated and utilized. Gain from a sale is generally eligible for the installment method, except for gain from the sale of inventory, cash basis receivables, and recapture income, which must be reported immediately.

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#### Taxable Sale of Ownership Interests

The taxable sale of ownership interests will generally result in one level of tax. Gain or loss is usually capital; however, the taxable sale of LLC interests may generate some ordinary income and installment method treatment might not be available to the extent of gain attributable to unrealized receivables and inventory.

**C corporation** – Capital gain. Gain from sale is generally eligible for installment method.

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**S corporation** – Capital gain. Gain from sale is generally eligible for the installment method. Possible Section 338(h)(10) election to get a step-up in the basis of assets. The election may trigger some ordinary income depending upon the character of the assets held by the S corporation at the time of sale.

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**LLC** – Capital gain. However, ordinary income to the extent of unrealized receivables and inventory. Gain from sale is generally eligible for the installment method, except for gain attributable to unrealized receivables and inventory, which must be reported immediately. Sale of 50% or more of the LLC within 12 months will cause a deemed termination and reconstitution of the LLC for tax purposes.

#### Availability of Qualified Small Business (QSB) Stock Incentives

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Subject to certain limitations, the exclusion of gain on QSB stock is 50%. However, gains on QSB stock are subject to a special tax rate of 28%, resulting in an effective rate of 14%. This provides a modest tax-advantage (compared to the 20% capital gains rate on non-QSB stock) at the cost of complying with certain statutory requirements. Past economic stimulus bills increased the exclusion to 75% for QSB stock acquired after February 17, 2009 and on or before September 27, 2010 resulting in a 7% effective tax rate. For QSB stock acquired after September 27, 2010 and before January 1, 2015, the exclusion is 100%, resulting in a 0% effective tax rate.

**C corporation** – Only shares of stock in a C corporation may be “qualified small business stock.” If certain requirements are satisfied, and subject to certain limitations, a taxpayer (other than a corporation) may (i) depending on when the QSB stock was acquired exclude from 50% to 100% of the gain (taxed at 28%) on the sale of qualified small business stock held for more than five years, or (ii) defer the gain on a sale of qualified small business stock by reinvesting the proceeds into another qualified small business.

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**S corporation** – Qualified small business stock incentives do not apply to stock issued by an S corporation, even if the S corporation converts to a C corporation.

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**LLC** – LLC equity is not eligible for QSB treatment. However stock issued to LLC members upon the conversion of an LLC to a C corporation is not precluded from being qualified small business stock by reason of the prior existence of the LLC. However, the holding period of qualified small business stock does not start until the former LLC members receive their shares in the qualified small business corporation.

#### Public Offering

Public offerings are typically made by C corporations. If a public offering is the likely exit strategy, but flow-through taxation is desired before then, the mechanics for an S corporation to become a C corporation (revoking S corporation status) are generally easier than changing an LLC to a C corporation (e.g. by merger, conversion, or consolidation).

**C corporation** – Can make a public offering.

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**S corporation** – Can make a public offering if S election is revoked.

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**LLC** – Cannot make a public offering. Must change to corporate status.

For more information please contact **Chip Wry**.

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#### Footnotes:

1. For purposes of this article, except as noted, the tax analysis relating to LLCs assumes that the LLC is a multi-member LLC taxed as a partnership. Thus, the LLC tax analysis in this article also generally applies to entities organized as partnerships. LLCs with a single member are typically treated as “disregarded entities” for federal income tax purposes.
2. Net investment income tax (“NIIT”) applies to certain investment income of high income shareholders at 3.8%.
3. The Massachusetts entity level tax rate for S corporations with total receipts in excess of \$9 million is equal to the difference between the corporate income tax rate and the individual

income tax rate and the rate for S corporations with total receipts between \$6 million and \$9 million at 2/3 of this difference. For 2015, these rates are 2.75% and 1.83%, respectively.

4. See footnote 2 above.

5. The Treasury and the IRS continue to consider this treatment in light of the requirements of the Affordable Care Act which generally prohibit employers reimbursing employees for individual health insurance premiums.

6. See footnote 2 above.