



Startup Law Blog

Insights for founders of and investors in emerging and startup companies

[Choice of Entity: Is An LLC OK?](#)

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I am frequently asked by entrepreneurs what type of entity they should form. And I usually advise startups to form as either a C corporation or an S corporation for the following reasons:

- If you plan to grant stock options to employees or contractors, it is much easier to do this through a corporation than an LLC taxed as a partnership.
- If you plan to raise funds from third parties in the future, investors typically don't want to invest in a pass through company and receive a Form K-1, and so it typically makes sense to start as a corporation (and if you elect S corporation status, terminating it prior to a fund raise is easier than converting an LLC to a corporation prior to a fund raise).

I think the advice is pretty typical of what startup entrepreneurs hear. In fact, I think the mantra from organizations around town is to form a corporation for your new business. However, it is not always the case that an LLC is a bad choice. I met with an entrepreneur recently who was going to form a new company to test an idea, to see if it had legs. He was going to be the initial, sole owner of the business. And he didn't know what he was going to discover. He didn't know if in 6 months he'd have a business or not, and one in which he would probably want to raise third party money for. In this situation, forming an LLC can be a good, inexpensive way to get started. Why?

- Single member LLCs are inexpensive to form. All you need to do is file a Certificate of Formation with the Secretary of State. If it is a single member LLC, you don't even need an LLC agreement (although you can easily and inexpensively put one together if you like).
- If you aren't initially going to have employees, you don't even have to obtain a separate taxpayer identification number for the company. You can use your SSN.
- Your income and loss will be reported on your Form 1040--meaning you don't have the expense and burden of filing a separate US corporate income tax return.
- If you later decide you want to raise third party money and/or grant equity compensation to service providers, and you don't intend to lever the business with a lot of debt in the meantime, conversion is relatively inexpensive and painless.



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Of course, you will need separate bank accounts and financial statements for the business in any event, regardless of what type of entity you form.

In conclusion, even if you get advice that you form a corporation for the reasons recited above, it is not necessarily the right answer for you, and it is worth considering the question as to what is the best approach before deciding.

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