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|-----------------|-----|-----|------------------------------------|------------------------------------|---|
| Disguised Sales | N/A | N/A | Same as Limited Liability Company. | Same as Limited Liability Company. | Where contribution and distribution appear to be related, the two transactions will be recharacterized as a sale; regulations presume that transactions occurring within two years are related. IRC § 707(a)(2); Prop. Reg. §1.707-3. |
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| Consideration | C Corporation | S Corporation | General Partnership | Limited Partnership | Limited Liability Company |
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|---|--|--|-----------------------------------|-----------------------------------|-------------------------------------|
| Availability of Tax-Free Contribution to Capital Provision by Non-Owner Under §118 ¹ | Yes | Yes | No | No | No |
| Interest Acquired for Services | Yes, unless IRC § 83 defers recognition. | Yes, unless IRC 83 defers recognition of profits interest. | Same as Limited Liability Company | Same as Limited Liability Company | Yes, but can structure partnership. |

¹Code §118 allows a corporation to exclude from income contributions from non-owners. This provision is often used by corporate tenants who receive cash allowances for tenant improvements from landlords as support to exclude such allowances from income. See The May Department Stores, TC Memo 1974-253, aff'd 8th Cir., Federated Department Stores, 51 TC 500 (1968), aff'd 6th Cir., and Elder-Beerman Stores Corp., Case No. 95-33643, Bankr. S.D. Ohio (3/20/97). But see IRS ISP Coordinated Issue Paper for the Retail Industry, 96 TNT 199-13 (10/7/96).

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| Effect of ownership interest for services | Will defeat tax-free transfer for other transferors when service provider obtains in excess of 20% of the stock; de minimis transfers (less than 10% of value of services) of property by service provider will not alter rule; service provider taxed on fair market value of the stock under IRC 83, Treas. Reg. § 1.351-1(a)(1), and Rev. Proc. 77-37, 1977-2 CB 568, §3.07. | Same as C Corporation. | Same as Limited Liability Company. | Same as Limited Liability Company. | No effect on tax-free transfers of other transferors; service member taxed on receipt of a capital interest (current deduction or capital expenditure to capital-relinquishing partners and gain if capital is appreciated), but service partner is generally not taxed on receipt of a profits interest. (Campbell v. Comm'r, 943 F2d 812 (8 th Cir. 1991)). |
| Taxation of Built-In Gain on Property Contributed | No | Yes, where converted from a C corporation, if the property is disposed of within 10 years. Corporation pays tax. §1374. | Same as Limited Liability Company | Same as Limited Liability Company | No, but any built-in gain or loss must be allocated to the contributing partner. §704(c). |
| Availability of Shifting Pre-Contribution Gain or Loss to Other Owners | Not applicable | Yes | No ² | No | No |

²IRC §704(c) requires that pre-contribution gain or loss be allocated to the contributing partner or member.

| Consideration | C Corporation | S Corporation | General Partnership | Limited Partnership | Limited Liability Company |
|---|---|---|-----------------------------------|--|---|
| Distribution of Refinancing Proceeds | Generally taxable | Generally taxable | Generally not taxable | Generally not taxable, even to limited partners if nonrecourse debt. | Generally not taxable. |
| Entity Gain on Distribution of Appreciated Property | Generally, treated as a sale of property to the shareholder and gain taxed to the corporation. | Will be treated as a sale of property to distributee and gain taxable to shareholder. IRC §311(b). ³ | Same as Limited Liability Company | Same as Limited Liability Company | Generally tax-free ⁴ , unless distribution in satisfaction of dollar amount owed to partner. |
| Distributions in Redemption of Ownership Interests. | Taxable as dividends to individual to extent of E&P; then non-taxable to extent of basis with excess subject to capital gain. | Dividend distributions not taxable to extent of AAA account; ⁵ then reduced old C corporation's E&P, and then offsets stock basis. Balance is treated as capital gain. | Same as Limited Liability Company | Same as Limited Liability Company | Generally taxable only to the extent of cash in excess of basis. ⁶ |

³IRC §311(b). If a C corporation converts to an S corporation and built-in gain exists, a distribution of the property within 10 years can result in gain to the S corporation. IRC §1374.

⁴The distribution of marketable securities can result in gain to the extent that they are in excess of the distributee's tax basis in the partnership. IRC §731(c). Also, if property is distributed to a partner and that partner has contributed property to the partnership, the distributee partner may have gain under IRC §737. In addition, the distribution of property to a partner and a transfer of money or other consideration by that partner to the partnership may result in a disguised sale. Reg. §1.707-6. Also, if property is contributed to a partnership and within 7 years the property is distributed to another partner, the contributing partner may have gain under IRC §704(c)(1)(B).

⁵The Accumulated Adjustment Account, referred to as the "AAA account", is generally undistributed earnings of an S corporation since its S election that have been previously taxed to the shareholder.

⁶Distributions do not result in taxable income unless (1) the distribution is of money and exceeds the partner's basis in the partnership interest, (2) the share of a partner's liabilities decreases as a result of the distribution and the decrease exceeds the partner's basis in the partnership interest, (3) a partner contributes appreciated property and within two years receives a distribution, unless he can establish that the transaction was not a disguised sale, (4) a partner contributes appreciated property which is distributed to another partner within seven years, (5) under certain circumstances, a partner contributes appreciated property, and the partnership makes a distribution of other property to the contributing partner within seven years after the contribution

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| Liquidating Distributions | Taxable to both corporation and shareholder. | Generally not taxable to corporation but taxable to shareholder. §311(b). ⁷ | Same as Limited Liability Company | Same as Limited Liability Company | Not taxable to the extent of basis. |
| Availability of Dividends Received Deduction. | A C corporation can exclude 70 percent of qualifying dividends from income (80 percent if the investor corporation holds 20 percent or more of the stock. ⁸ A C corporation can file a consolidated return, if it is a member of the affiliated group. | An S corporation is not entitled to the dividends received deduction, nor may it file a consolidated return with any other entity. However, the income of certain wholly owned subsidiaries can be treated as directly owned by the parent S corporation. IRC §1361(b)(3)(A). | None. | None. | None. |
| Transfer Tax on Property Transferred To/From ⁹ | Generally none. | Generally none. | Generally none. | Generally none. | Generally none. |

while it is still holding the contributed property, or (6) the distribution is a guaranteed payment.

⁷For exception, see note 25.

50 IRC §243.

⁹Many states, counties and cities impose a transfer tax on the transfer of property. Although transfers to controlled entities are generally exempt, the specific rules of each political subdivision should be consulted.

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| Redemption of Owner | Taxable as if stock sold, unless treated as a dividend under IRC §302(b). | Taxable as if stock sold, unless treated as a dividend under IRC §302(b). | Same as Limited Liability Company. | Same as Limited Liability Company. | Can be structured either of two ways. ¹⁰ |
| Character of Gain or Loss on Sale of Interest in Entity | Capital if held more than 1 year, unless collapsible corporation under §341 or dealer property. | Capital if held more than 1 year, unless collapsible corporation under §341 or dealer property. | Same as Limited Liability Company | Capital except to the extent the partnership has so-called “hot assets”. | Capital except to the extent the partnership has so-called “hot assets”.. ¹¹ |
| Items of Income in Respect of a Decedent (IRD) in the Entity’s Basis Adjustment at Death | Items of IRD held by a corporation has no effect on the adjustment in the shareholder’s basis of his stock upon his death. | Same as Limited Liability Company | Same as Limited Liability Company | Same as Limited Liability Company | No basis adjustment is available for an interest in the entity to the extent that the value of the interest consists of a pro rata share of IRD. ¹² |
| Subject to Personal Holding Company Tax | Yes if a personal holding company. | No | No | No | No |

¹⁰Redemption payments may be treated either as a payment for property or as a distributive share of partnership income (or guaranteed payment) with different consequences to the partnership and the redeemed partner. IRC §736. General partners can be treated differently from limited partners in connection with payments for unrealized receivables and goodwill. IRC §736(b)(3).

¹¹“Hot assets” include depreciation recapture, unrealized receivables, and inventory. IRC §751. For sales prior to August 5, 1997, inventory had to be “substantially appreciated” to qualify as a “hot asset”. For distributions under §751, inventory still must be substantially appreciated.

⁵⁴ IRC §1014(c); Reg. §1.742-1; see also Woodhall v. Commissioner, 454 F. 2d 226 (9th Cir. 1972); Rev. Rul 66-325, 1966-2 C.B. 249. Applies to S corporations with respect to decedents dying after August 20, 1996.

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| Method of Accounting | Cash ¹³ or accrual | Cash or accrual | Same as Limited Liability Company. | Same as Limited Liability Company. | Cash or accrual, unless the entity has a C corporation as an owner, or is a tax shelter, as defined by IRC §461(i)(3), and does not meet any of the exceptions. IRC §448(d)(3). |
| Form for Reporting Income | Form 1120 | Form 1120S | Form 1065 | Form 1065 | Form 1065 ¹⁴ |
| Choice of Taxable Year | Any C corporation (which is not a personal service corporation) can elect a calendar year or any fiscal year as its taxable year. | Generally calendar year, unless IRC §444 election made. | Same as Limited Liability Company. | Same as Limited Liability Company. | Must have taxable year of the majority member partner or of all the principal partners; otherwise, a calendar year unless IRC §444 is elected. |

¹³ A C corporation can use the cash method only if its three-year moving average of gross receipts has never exceeded \$5 million. IRC §448(b)(3). Also, qualified personal service corporations may use the cash method. IRC §448(b)(2).

¹⁴ The “check-the-box” regulations issued on December 17, 1996, permit an entity that has only one member to elect to be classified as a corporation or to be disregarded as an entity separate from its owner (i.e., a sole proprietorship, division or branch); if single member LLC does not elect to be classified as a corporation, all items of income and expenses and the assets and liabilities will be included in the return of the single member.

