Limited Liability Company - LLC

What is a Limited Liability Company - LLC

A limited liability company is a corporate structure whereby the members of the company are not personally liable for the company's debts or liabilities. Limited liability companies are hybrid entities that combine the characteristics of a corporation and a partnership or sole proprietorship. While the limited liability feature is similar to that of a corporation, the availability of flow-through taxation to the members of an LLC is a feature of partnerships.

BREAKING DOWN Limited Liability Company - LLC

Although LLCs have some attractive features, they also have several disadvantages, especially in relation to the structure of a corporation. Depending on state law, an LLC may have to be dissolved upon the death or bankruptcy of a member, unlike a corporation, which can exist in perpetuity. Also, an LLC may not be a suitable option when the founder's objective to become a publicly listed company, eventually.

The primary reason business owners opt to take the LLC route is to limit the principals' personal liability. Many view an LLC as a blend of a partnership, which is a simple business formation of two or more owners under an agreement, and a corporation, which has certain liability protections. An LLC is a more formal partnership arrangement requiring articles of organization to be filed with the state. An LLC is much easier to set up than a corporation, and it provides more flexibility along with the protection. However, creditors may still pierce the corporate veil of an LLC in cases of fraud or when a company hasn't met legal and reporting requirements.

Differences between a Partnership and a Limited Liability Company

The primary difference between a partnership and an LLC is that an LLC separates the business assets of the company from the personal assets of the owners, which insulates the owners from the LLC's debts and liabilities. An LLC functions similar to a partnership in that the profits of the company pass through to owners’ tax return. Losses can be used to offset other income, but only up to the amount invested. The LLC only files an informational tax return.

In terms of the sale or transfer of the business, a business continuation agreement is the only way to ensure the smooth transfer of interests when one of the owners leaves or dies. Without a business continuation agreement, the remaining partners must dissolve the LLC and create a new one is a partner files bankruptcy or dies.