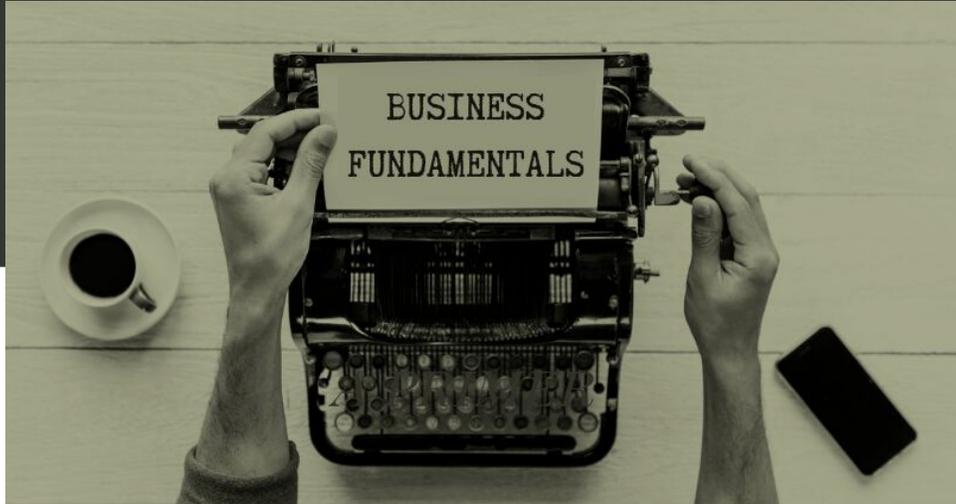


Business Fundamentals: California Corporations

01.09.18 | Linda J. Rosenthal, JD



A corporation is a useful way to start a new business, because as soon as you file the business' Articles of Incorporation, the new business entity immediately becomes a separate legal entity with many of the legal rights of an individual.

The choice to form a corporation, rather than conduct business as a Sole Proprietorship or Limited Liability Company, could be based on liability concerns, tax considerations, or capitalization needs. In California, there are five primary factors to consider once you've decided to form a corporation:

- What you want your business name to be;
- Who should serve as your "registered agent";
- How the business should be viewed by the IRS (S-corp a C-corp);
- Who will own the business (shareholders), and who will manage it (board of directors)?
- Does the business need to register with the Securities and Exchange Commission (SEC), the California Department of Business Oversight, or other licensing agency?

Corporate Business Name

The name that you select for your business is crucial – and must be original. The California Secretary of State will not file Articles of Incorporation for a start-up that is too similar to an already existing corporation. Further, an internet presence is important for most businesses, and if the domain name is already in use by someone else, you may have a problem with branding.

Finally, your name must be original to avoid infringing upon the Trademarks, Service Marks, or Copyrights of other businesses

Our attorneys are quickly able to check and reserve a proposed name with the California Secretary of State, and we can ensure your domain is available (if you haven't already), and also perform a simple name check with the United States Patent and Trademark Office to further clear the use of your proposed name.

Registered Agent in California

When filing Articles of Incorporation, the California Secretary of State requires a new business to name someone located in the state of California who consents to accepting service of process (legal documents), and who will forward them to the business in a timely fashion.

Any resident individual, and some firms including ours, can serve as a registered agent for businesses in California. However, the requirements of the agent include having a California street address, and being available at that address during normal business hours.

Decide Between C-corp and S-corp Designation

The tax default for every new corporation is as a C-corp. To elect to be treated as an S-corp, the new entity must file a request for tax treatment as an S-corp with the IRS within 60 days of formation.

As a separate legal entity, the C-corp is separately taxable, and files a separate taxable return (1120) and pays taxes on the business' earnings. This can lead to "double" taxation when the income is distributed to the owners as dividends upon which they are taxed at the individual rate.

The S-corp is a pass-through tax entity. S-corps file an informational federal return (Form 1120S), but no income tax is paid at the corporate level. Then, the profits or losses of the business are instead "passed-through" the business and reported on the owners' personal tax returns. Any tax due is paid at the individual level by the owners.

Because of this preferential tax treatment, there are some restrictions on S-corps. While C-corps have no restrictions on ownership, S-corps do. S-corps are restricted to no more than 100 shareholders, and shareholders must be US citizens or legal residents. S-corps cannot be owned by C-corps, other S-corps, LLCs, partnerships or many trusts. Also, S-corps can issue only one class of stock (disregarding voting rights), while C-corps can have multiple classes of stock.

Who Will Own and Manage the Corporation

Ownership of a corporation is through the "stock" of that corporation. Owners purchase a number of "shares," and hold their "share" of the corporation's value.

The incorporator (the person who signed the Articles of Incorporation) is responsible for appointing the initial corporate directors. These individuals will set on the board of the new corporation until they (or new members) are elected by the shareholders during the initial meeting of the shareholders of the corporation.

If the corporation is small, the shareholders should prepare and execute a shareholders, or "buy-sell" agreement. This contract provides that if the shareholder dies, or wants to sell his or her stock, it must first be offered to the surviving shareholders.

Registration and Licensing

All California corporations who issue securities (shares) are subject to the [California Department of Business Oversight \(DBO\)](#). If a corporation is small, and only issuing a small number of shares to only a few owners, the DBO offers a limited offering exemption to the more onerous filings required of larger corporations.

If a corporation is large, and sells its shares to many individuals, the corporation will likely have to

register with both the Securities and Exchange Commission (SEC) and the California DBO.

Finally, depending on the type of business your corporation will be conducting, the state of California and many of the counties and cities within the state, may require you to obtain various licenses to operate, including sellers permits that are obtained through the California Board of Equalization (BOE).

Our attorneys understand the needs and goals of business owners, and can guide you through the confusing process of forming your California Corporation. Contact us for your free 20-minute consultation.