Types of Corporations

by Sophia

WHAT'S COVERED

We've talked about sole proprietorships in earlier lessons, but what happens when you don't want to be a sole proprietorship anymore? This tutorial provides an introduction to corporate ownership and types of corporations. Our discussion breaks down as follows:

1. The Corporate Alternative

A **corporation** is defined as an organization that legally operates as a separate entity. Before, with a sole proprietorship or partnership, the owners of the business and the business itself were indistinguishable. In this case, with a corporation, they are two separate entities.

Corporations can be large or small. They don't have to be the big-named ones that you may think of, like AT&T.

They also have different rights than other businesses because they are legally considered a person.

EXAMPLE The Supreme Court case of *Dartmouth College v. Woodward* in 1819 set this precedent. In the opinion written by Chief Justice Marshall, it stated that a corporation is an artificial being--invisible, intangible, and existing only in contemplation of law.

To have personhood means several things, including:

- A corporation can sue or be sued.
- It can run a business or attempt to earn a profit through the sale of goods and services.
- It can own, buy, or sell real estate.
- It can lend and borrow money.
- It can donate to political campaigns or causes.
- It can sign enforceable, binding contracts.

Let's take a look at some advantages and disadvantages of being a corporation.

Corporation	
Advantages	**Disdvantages**
Limited liability because, as a separate entity, the owners of the corporation are shielded	Dual taxation because they're a separate entity, the business profits are taxed, and then any distributions to the owners

from liability and lawsuits that arise from the operation of business.	are taxed as well.
Continuity because if an owner dies, you simply sell their share of the ownership to someone else. Because it's a separate entity, the business goes on.	Decision making can be a problem because the owners may not always agree with how the business is being run by the people they've hired that specialize in management.
Easy to raise money.	Tender offers are a constant threat to the owners of a business. To buy a corporation that's publicly held, all one has to do is acquire a majority of the shares of stock, and any one person or entity can do this.
Change of ownership is quite easy because all you have to do is sell your share of ownership to someone else.	Regulations because the U.S. government very heavily regulates corporations.
Specialized management that is hired by the board of directors to run the business.	Lack of secrecy because, if you're publicly held, you are required by law to divulge certain financial and company operations information every year.

TERM TO KNOW

Corporations
An organization that can legally operate as a separate entity.

2. Corporate Ownership

Corporate ownership is represented by shares of **stock**, which is a form of partial ownership of a corporation. Stock is owned by **stockholders**, the people who own the shares of stock for a corporation.

Corporations can be publicly owned or privately owned. A publicly owned corporation is owned through publicly traded shares like we just discussed, whereas privately owned corporations are owned by a defined group of investors and they're not publicly traded.

Stockholders, as owners of a company, have certain rights. This largely depends on the type of stock that they have.

- Common stock has voting rights, so they can vote on who gets to be on the board of directors and how the business is run. They're also issued dividends and because they're stockholders, that stock represents ownership in the company. If you, as a stockholder, can't get to the annual meeting to cast your votes, you can vote by proxy. **Proxy** is simply voting rights that are passed on to someone so he or she has the authority to act on behalf of the stockholder.
- Preferred stock is non-voting. They don't get a direct say in how the business is run. The benefit of having preferred stock is that any dividends that are paid are paid to preferred stockholders before common stockholders; therefore, they have priority in the earnings of the business. A **dividend** is a payment of earnings to shareholders from an organization. Profits that come from the business that are distributable to the shareholders are paid out through dividends attached to each share of stock.

TERMS TO KNOW

Stock
A form of partial ownership of a corporation.

Stockholders
People who own shares of stock for a corporation.

Proxy
Voting rights that are passed on to someone so he/she has the authority to act on behalf of the stockholder.

Dividend
A payment of earnings to shareholders from an organization.

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3. Corporate Governance

Corporate governance is simply the structures of rules, rights, and processes which govern a corporation. Let's take a look at the basic corporate structure.

Stockholders

Board of Directors

Corporate Officers

Employees

In the basic hierarchy of a corporation, the stockholders are first. They are the owners of the business--it's *their* business. They get a very definite say in who runs the business, and they do this by appointing or electing a board of directors.

The board of directors is in charge of the strategic vision of the business. They also hire the corporate officers who do the day to day operation of the business and are responsible for running it and making a profit for the shareholders.

Last, are the employees; everyone below the corporate officers are considered simply employees. These are the people who manage, produce, and sell the different products and services that are offered by the business.

THINK ABOUT IT

How do you become a corporation? First of all, consult a lawyer. This could be a fairly complicated process. It's also important to note that you can incorporate in any state that you like. You don't have to incorporate in the state you're doing business in. The primary reason people look to different states is that there's a large difference in cost and regulation. Delaware and Nevada are the most popular--they're considered very corporation-friendly.

TERM TO KNOW

Corporate Governance
The structures of rules, rights, and processes which govern a corporation.

4. Types of Corporations

There are many different types of corporations:

Type of Corporation	Description
S-Corporation (S-Corp)	Privately held and pass through income to shareholders. Typically are smaller organizations.
Limited Liability Corp (LLC)	Unique and the most varied of the different types of corporations. Blends elements of corporate and partnership structures. Can be small, even individuals, or single owners, who have incorporated up to larger businesses.
Professional Corporation	Typically lawyers and law firms. Must identify themselves with PC at the end of their corporate name.
Multinational Corporation	Larger companies, like Ford Motor Company, AT&T, and Microsoft, that do business worldwide.
Non-Profit Corporation	Treated differently for tax purposes. Don't pay federal taxes, because their primary goal is not making a profit. Banned from making a profit. All profits must go back into the business, which is fine because their primary goal isn't profit-motivated; rather, it's another cause.

There are some other types of corporations that you may not have heard of. They are typically characterized by the location where they operate and are headquartered.

- Domestic Corporations: Does business and incorporated in the same state
- Foreign Corporations: Does business in one state, but incorporated in another
- Alien Corporations: Does business in a given state, but incorporated in a foreign country

SUMMARY

Today, we learned about **the corporate alternative**, and what it might take to become a corporation. We also looked at **corporate ownership** and the corporate structure that ensures the smooth running of a corporation: the stockholders, the board of directors, the corporate officers, and the employees. We learned about the different **types of corporations**, like the S-corporation, the limited liability corporation, and the professional corporation. Lastly, we learned about **other types** of corporations that are lesser known, such as those that are primarily geographic-based or non-profit in nature.

Good luck!

Source: ADAPTED FROM SOPHIA INSTRUCTOR JAMES HOWARD

TERMS TO KNOW

Corporate Governance
The structures of rules, rights, and processes which govern a corporation.

Corporations
An organization that can legally operate as a separate entity.

Dividend
A payment of earnings to shareholders from an organization.

Proxy
Voting rights that are passed on to someone so he/she has the authority to act on behalf of the stockholder.

Stock
A form of partial ownership of a corporation.

Stockholders
People who own shares of stock for a corporation.