
Converting an S Corporation to a C Corporation

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Are you considering converting your S corporation to a C corporation? Let's go over some frequently asked questions that can help you decide if converting is right for you.

First, let's cover the basics: what is the difference between an S corporation and a C corporation?

An S corporation is taxed similarly to a partnership or sole proprietorship. The business's income and losses are passed through to the shareholders and reported on their individual tax returns.

A C corporation is taxed as its own separate entity. This means that the business pays its own taxes on any income it generates, and then the shareholders pay taxes on any dividends they receive.

Some benefits of converting to a C corporation may include greater flexibility, the ability to issue multiple classes of stock, and the potential for lower taxes.

C corporations have more options in raising capital, including the ability to issue stocks and bonds. Unlike S Corporations, a C Corporation is not restricted by the number nor types of shareholders it can have.

S and C corporations both provide shareholders with limited liability protection, but C corporations are also able to issue multiple classes of stock.

It can also be more tax efficient for a business to be taxed as a C corporation. For example, it may be beneficial for it to pay taxes at the corporate rate of 21%, rather than passing the income through to shareholders who would have to pay taxes at their individual rates. However, keep in mind that any distributions from a C Corporation are taxable to the shareholders as dividends.

To convert from an S Corporation to a C Corporation the process is relatively simple, but there are a few steps that you need to follow.

To become a S Corporation an entity would have previously filed a S election on Form 2553. To revoke this, the corporation needs to file a statement with the IRS Service Center where

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the corporation previously filed Form 2553. The statement needs to be signed by a person authorized to sign the entity's tax return and must provide a variety of information including:

- That the corporation is revoking its election under Sec. 1362(a) to be taxed as an S Corporation
- The name and address of the shareholder(s)
- The number of shares of stock owned by the shareholders
- The effective date of the revocation

Signature and consent of the shareholder(s) who collectively own more than 50% of corporation must also be provided with the statement of revocation.

A proper revocation of an S election can become effective on any specified date on or after the day on which the revocation is filed. It can even be retroactive to the beginning of the tax year if filed on or before the 15th day of the third month of the tax year.

Talk with your accountant to determine if converting to a C Corporation makes sense for your business.

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