An S Corporation is a form of business classified for federal income tax purposes as a corporation that has elected to be taxed as a pass-through entity, in a manner similar to a partnership or sole proprietor. Unlike a regular corporation, or C corporation, an S corporation (both names derive from sections of the Internal Revenue Code) generally is not subject to federal income tax. Instead, its income is reported on the tax returns of its shareholders, and they have the responsibility for paying the tax. If there are losses suffered by the corporation, they also pass through and are reported on the shareholders' income tax returns.

Because only the shareholders, and not the corporation, are taxed, S corporations avoid the problem of double taxation associated with C corporations. This is the biggest draw for creating an S corporation, particularly for closely held corporations.

Shareholders in an S corporation, like shareholders in a C corporation, generally have limited liability arising from corporate matters, even though they pay taxes as if they were partners or sole proprietors. In addition, when the corporation eventually is sold, there can be reduced taxable gains, as compared with the sale of a business operating as a C corporation.

On the downside, the limitation on classes of stock in an S corporation provides less control over the company and the value of its stock. Potential outside investors likely will not be attracted by the pass-through tax characteristics of an S corporation, nor by the limit on the number of shareholders. Although corporate taxes are avoided, there is still a requirement for filing an informational tax return every year for a corporation with more than one owner. Finally, if avoiding formalities is an important consideration, it should be noted that, like any other corporation, an S corporation must follow the requirements for having regular meetings and keeping company minutes.

The balancing of the advantages and drawbacks of S corporation status in any given case is sufficiently complex that it is advisable to seek professional advice before making this important choice.

TAX CREDITS FOR HISTORIC PRESERVATION

For over 30 years, the federal government has been using tax incentives to help preserve historic buildings. Originally, federal law allowed accelerated depreciation on rehabilitated buildings, but subsequent changes have made preservation and revitalization efforts even more attractive to taxpayers.

Today, there is a general business credit equal to 20% of qualified rehabilitation expenses for a certified historic structure, or a 10% tax credit for the qualified rehabilitation of non-historic, nonresidential buildings first placed into service before 1936. Eligibility for the tax incentives is determined by the National Park Service.

Tax credits are often more beneficial to taxpayers than deductions are, since every dollar of a tax credit reduces the amount of income tax owed by one dollar.

The 20% credit for the rehabilitation of a certified historic structure applies to commercial, industrial, agricultural, rental, or residential properties, but not to properties used exclusively as the owner's private residence. A certified historic structure must be a building as opposed to another type of structure. To have the required historic status, the building must be either listed individually in the National Register of Historic Places or located in a registered historic district and certified as being of historic significance to the district.

Eligibility for the 20% credit also depends on meeting some additional requirements. For example, the building must be depreciable, that is, used in a trade or business or held to produce income. The rehabilitation must be substantial, generally defined as entailing expenditures exceeding the adjusted basis of the building and its structural components. Generally, this requirement must be met within two years or within five years for a project completed in multiple phases.

Qualified rehabilitation expenses include such items as architectural and engineering fees, site survey and development fees, legal expenses, and other construction-related costs, so long as they are added to the basis of the property, are reasonable, and are related to services performed.

The owner of the rehabilitated building must hold it for five years after completion of the rehabilitation or else pay back all or part of the 20% credit. A sale in the first year means that the entire credit is recaptured. The recapture amount is reduced by 20% per year for properties held between one and five years.

The 10% credit for non-historic buildings constructed before 1936 shares some of the requirements for the 20% credit, such as that the rehabilitation be substantial and the property be depreciable. However, only buildings rehabilitated for nonresidential uses qualify for the 10% credit. In addition, so that the identity of the original building is not lost in the process, projects undertaken for the 10% credit must meet specific tests based on retention of minimum percentages of the building's walls and internal structural framework.