

CARBON LAW GROUP PRESENTS

YOUR CALIFORNIA BUSINESS BLUEPRINT

The Founder's Guide to Choosing the
Right Legal Entity & Building a Solid
Foundation in California

INSIDE THIS GUIDE

- ☒ How to choose between LLC, S-Corp, C-Corp, and Sole Proprietorship
- ☒ California-specific rules, taxes, and compliance requirements
- ☒ A step-by-step Founder's Launch Checklist (35 items)
- ☒ Critical next steps to protect your business from day one

INTRODUCTION

Why Entity Selection Is the Most Important Decision You'll Make as a Founder

Starting a business in California is an exciting step. But before you send a single invoice, hire your first employee, or sign your first contract, one decision will shape nearly every aspect of your business: choosing the right legal entity.

The entity you choose determines how you are taxed, how much personal liability you carry, how you raise capital, and how your business is managed day to day. Getting this wrong – or delaying the decision – can cost you tens of thousands of dollars and years of legal headaches.

The Most Common Founder Mistakes

Operating as a sole proprietor without knowing it. Choosing an LLC when a C-Corp is required for VC funding. Forming in Nevada or Wyoming to “avoid California taxes” – only to discover California still taxes you. Mixing personal and business finances from day one. **This guide helps you avoid every one of these mistakes.**

What This Guide Covers

- A plain-language breakdown of the four main entity types available to California founders
- A side-by-side comparison of liability, taxation, management, and formation cost
- California-specific rules, fees, and franchise tax obligations you must know
- A complete Founder's Launch Checklist to keep your formation on track
- Clear next steps and how Carbon Law Group can guide you through each one

This guide is for informational purposes only and does not constitute legal advice. Every business situation is unique. The information reflects California law as of 2025 and is subject to change. Consult a licensed attorney before making formation decisions.

ENTITY OVERVIEW

The Four Main Entity Types — Side by Side

Each entity type carries distinct legal, tax, and operational implications. Use this comparison as your starting point.

	Sole Prop.	LLC	S-Corp	C-Corp
Liability Protection	No separation — full personal exposure	Strong — members shielded from business liabilities	Strong — shareholders protected	Strong — shareholders protected
Formation Cost (CA)	None — automatic	\$70 filing fee + \$800/yr min. tax	\$100 filing + \$800/yr min. tax	\$100 filing + \$800/yr min. tax
Taxation	Pass-through via Schedule C	Pass-through (default); can elect S-Corp taxation	Pass-through; self-employment tax savings possible	Double taxation; 21% flat federal rate
CA Franchise Tax	None	\$800/yr minimum	\$800/yr minimum	\$800/yr minimum
Ownership	1 owner only	Unlimited members; any type	Max 100; US persons only	Unlimited; any investor type
VC / Investment	Not compatible	Uncommon	Not compatible with VC	Preferred structure for VC
Complexity	Minimal	Flexible; low overhead	Corporate formalities required	Board, officers, annual meetings
Best For	Freelancers testing an idea	Most small businesses & startups	Profitable cos. cutting S/E tax	High-growth, VC-backed startups

Quick Rule of Thumb

Testing an idea solo? ☑ Sole prop or single-member LLC. Building a team or signing contracts? ☑ LLC. Raising venture capital? ☑ Delaware C-Corp. Profitable with significant self-employment tax? ☑ Discuss S-Corp election with your attorney.

ENTITY DETAILS

Entity Deep Dive — What You Need to Know

Sole Proprietorship

Simplest structure — but highest personal risk

A sole proprietorship is not a separate legal entity. If you are operating a business under your own name without filing any formation documents, you are already a sole proprietor by default. Your personal assets — home, car, savings — are fully exposed to business debts and lawsuits.

ADVANTAGES	CONSIDERATIONS
Zero formation cost or paperwork	No liability protection — 100% personal exposure
Complete control; no partners or board	Harder to open business bank accounts
Simple Schedule C filing on personal return	No path to outside investment or adding partners

Carbon Law Group: Sole proprietorship is acceptable for very early-stage freelancers with minimal contract risk. Once you are signing commercial leases, hiring staff, or working with clients who could sue you, form an LLC immediately.

Limited Liability Company (LLC)

The workhorse of small business — flexible and protective

The LLC is the most common entity for California small businesses and startups. It separates personal assets from business liabilities while offering significant operational flexibility. California requires all LLCs to pay the \$800 annual minimum franchise tax — even if the business has zero income in its first year.

ADVANTAGES	CONSIDERATIONS
Strong personal liability protection for all members	\$800/yr CA franchise tax regardless of profit
Flexible management: member or manager managed	Self-employment taxes on full distributive share
Pass-through taxation by default; no double taxation	LLCs with revenue over \$250K pay gross receipts fees
Can elect S-Corp or C-Corp tax treatment	Not ideal for venture capital investment
No limit on number or type of members	

Carbon Law Group: For most founders building a service business, retail operation, or early-stage startup not seeking VC, a California LLC is the right default. We structure Operating Agreements to protect your ownership interest as you add partners or investors.

S-Corporation

The tax-efficient choice for profitable small businesses

An S-Corp is a federal tax election — not a standalone entity type — applied to a corporation or LLC. Its key advantage: owner-employees pay themselves a “reasonable salary,” and only that salary is subject to self-employment and payroll taxes. Remaining profit is distributed without those taxes, which can save thousands of dollars annually once the business is consistently profitable.

ADVANTAGES	CONSIDERATIONS
S/E tax savings on distributions above reasonable salary	Maximum 100 shareholders; must be US persons
Pass-through taxation; profits flow to personal return	Only one class of stock (no preferred shares)
No double taxation at the entity level	Requires corporate formalities: meetings and minutes
Credibility of a corporate structure	Incompatible with venture capital structures
	CA levies 1.5% franchise tax on net income (min. \$800)

Carbon Law Group: The S-Corp election typically makes sense when annual net profit exceeds approximately \$40,000–\$50,000. Below that threshold, compliance costs often outweigh the payroll tax savings. We model this specifically for each client before recommending the election.

C-Corporation

The standard for high-growth, venture-backed companies

A C-Corp is the entity of choice for startups intending to raise institutional capital. Venture capitalists and angel investors almost universally require a C-Corp — typically incorporated in Delaware, even if the company operates entirely in California. The tradeoff is double taxation: the corporation pays federal taxes at 21%, and shareholders pay again when dividends are distributed.

ADVANTAGES	CONSIDERATIONS
Unlimited shareholders; any investor type or entity	Double taxation on distributed profits
Multiple classes of stock for VC rounds	Highest admin burden: board, officers, annual meetings
Strong liability protection for all shareholders	California taxes on top of federal (\$800 min.)
Employee equity incentives (ISOs, options) straightforward	Delaware incorporation adds registered agent costs
21% flat federal rate (favorable for retained earnings)	Converting from LLC later is expensive and complex

Carbon Law Group: If you are building a technology company, scalable consumer brand, or any business where outside investment is part of the plan, incorporate as a Delaware C-Corp from day one. Converting later is expensive, complex, and can create significant tax complications.

CALIFORNIA COMPLIANCE

California-Specific Requirements You Cannot Ignore

California is one of the most regulated business environments in the United States. Founders frequently underestimate state-specific obligations — and the consequences of non-compliance include back taxes, penalties, suspension, and loss of good standing.

The \$800 Annual Franchise Tax

Every LLC, S-Corp, and C-Corp registered in California — or doing business in California — owes a minimum \$800 franchise tax per year to the California Franchise Tax Board (FTB). This applies even if your business earned zero revenue. LLCs formed after January 1, 2021 receive a first-year exemption. After that, it is due every April 15.

California Secretary of State Filings

Formation documents (Articles of Organization for LLCs; Articles of Incorporation for corporations) are filed with the California Secretary of State. LLCs must also file a Statement of Information (Form LLC-12) within 90 days of formation and every two years thereafter. Corporations file annually. Failure to file results in suspension.

LLC Gross Receipts Fee

California LLCs with annual gross revenues above \$250,000 owe an additional fee on top of the \$800 minimum: \$900 for \$250K–\$499K; \$2,500 for \$500K–\$999K; \$6,000 for \$1M–\$4.9M; \$11,790 for \$5M+. Plan for this in your year-one financial projections.

Registered Agent Requirement

Every California business entity must maintain a registered agent — a person or entity with a physical California address available during business hours to receive legal process (lawsuits, government notices). This cannot be a P.O. Box. You may serve as your own registered agent or use a professional service.

Employment & Payroll Compliance

If you hire employees, you must register with the California Employment Development Depart-

ment (EDD), withhold state income taxes, and comply with California's employee classification rules. AB 5 significantly restricts the use of independent contractors. Misclassification carries severe penalties – including back wages, penalties, and personal liability.

Business Licenses & Local Permits

California requires a seller's permit from CDTFA if you sell taxable goods. Most cities – including Chino Hills – require a local business license. Industry-specific licenses (contractors, health-care, financial services, food service) add another layer. Failure to maintain proper licenses can void contracts and expose you to fines.

Foreign Entity Registration

If you form your entity in another state (e.g., Delaware C-Corp) but operate in California, you must file a Foreign Corporation or Foreign LLC registration with the California Secretary of State and pay California franchise taxes. "Delaware incorporation to avoid California taxes" is a myth. California taxes you regardless of where you incorporated.

ACTION CHECKLIST

The Founder's Launch Checklist

Use this checklist to track every critical step from idea to fully compliant, operational business. Check each item off as you complete it – or bring it to your discovery call and we will walk through it together.

Phase 1 – Before You Form

- [] Define your business model: product/service, customer, revenue model
- [] Run a CA Secretary of State name availability search
- [] Search USPTO trademark database for name conflicts
- [] Identify co-founders and agree on ownership percentages in writing
- [] Determine funding strategy: bootstrapped, angel, or VC
- [] Consult an attorney to select the right entity

Phase 3 – Banking & Finance

Phase 2 – Formation

- [] File Articles of Organization (LLC) or Articles of Incorporation (Corp) with CA SOS
- [] Obtain EIN from the IRS – free at irs.gov
- [] Designate a California registered agent
- [] Draft and execute Operating Agreement (LLC) or Bylaws + Shareholders Agreement (Corp)
- [] File Statement of Information within 90 days
- [] Register with CA FTB; pay initial \$800 franchise tax
- [] Delaware C-Corp: file Foreign Corp registration with CA SOS
- [] Open dedicated business checking account (bring EIN, formation docs)
- [] Set up separate business credit card – never commingle funds
- [] Configure accounting software (QuickBooks, Xero, or similar)
- [] Establish chart of accounts from day one
- [] Review startup costs for deductibility under IRC §195

Phase 4 — Licenses & Permits

- [] Obtain city business license (Chino Hills or relevant municipality)
- [] Register with CA CDTFA if selling taxable goods
- [] Obtain all industry-specific California state licenses
- [] Register with CA EDD if hiring W-2 employees
- [] Confirm zoning compliance for your business location
- [] Review AB 5 rules before engaging independent contractors

Phase 5 — IP & Contracts

- [] File federal trademark application(s) for business name and logo
- [] Draft or review your core client services agreement

- [] Implement NDA template for vendor and partner conversations
- [] Establish IP assignment agreements for all creators of work product
- [] Review website: privacy policy, terms of use, cookie notice

Phase 6 — Annual Compliance

- [] Pay CA franchise tax by April 15 each year (\$800 minimum)
- [] File biennial Statement of Information (LLCs) or annual SI (Corps)
- [] Maintain meeting minutes for board/member meetings
- [] Renew local business licenses annually
- [] Review Operating Agreement any time ownership changes
- [] Schedule annual legal review with your attorney

Let's Make Sure We're the Right Fit for Each Other.

We work best with founders who are serious about building the right way. A quick discovery call lets us both decide if Carbon Law Group is the right partner for where you're headed.

What Happens on the Discovery Call

Book directly at: pk-carbonlg.zohobookings.com

- ☒ 15-20 minutes – focused, no fluff, respectful of your time
- ☒ You tell us about your business – where you are, where you're headed, and what's keeping you up at night
- ☒ We tell you honestly whether we're the right fit and what working together would look like
- ☒ If it's a match, we'll outline a clear path forward – entity selection, formation, and beyond
- ☒ If it's not, we'll point you in the right direction – no hard sell, ever

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We Serve

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