

Choosing a Business Structure

WHAT ARE MY CHOICES?

Sole Trader — A sole proprietorship is the simplest and most common form of business structure. It is owned by one person who retains all of the legal rights and bears all of the responsibilities associated with the business. The owner enjoys all the profits flowing from the business and is responsible for all of its debts. The income of the business is reported as personal income on the owner's personal income tax return.

Partnership — A partnership is established when two or more people agree to pool their resources in order to operate a business for profit. Each partner owes every other partner a duty to act in the best interests of the partnership. Like a sole proprietor, a partner's share of the partnership's income is recorded on each individual partner's personal income tax return. It is essential that a Partnership Agreement is signed by all partners to help in regards to settlement of any disputes that may arise in connection with the business.

Company — A business may operate as a separate legal entity in the form of a company. This is a more complex form of business structure governed by Corporation Law, which covers how a company operates and the duties of the directors. A company must register a company name with the Australian Securities and Investments Commission (ASIC) and pay an annual fee (approximately \$212) to them in order to keep the company trading.

Unit Trust — A Unit Trust is not a separate legal entity in the same way as an individual or a company, rather it is a relationship which exists whereby a person (Trustee) is compelled to hold property for the benefit of others (Beneficiaries or Unitholders). The relationship is formalized to the extent the units are held by the beneficiaries and the rights attached to such units can be structured in a similar fashion as shares in a company.

Discretionary Trust — Unlike a Unit Trust, you establish a Discretionary Family Trust to benefit the members of a family. Discretionary Family Trusts provide families with a great deal of flexibility in sharing the tax burden among family members and protecting family assets. The Discretionary Family Trust structure is useful if your family holds capital growth or income-generating assets and can last up to 80 years.

WHICH ONE DO I CHOOSE?

The choice of a business structure is one area where you should seek professional advice from your accountant. You should make sure you understand the advantages and disadvantages of each type of structure before you make the decision. All aspects of each structure should be explored and a choice made which best suits the way you intend to run the business. More detailed information about the advantages and disadvantages of each structure are located in the following pages.

HOW DO I SET UP THE BUSINESS?

Once you have decided what structure you would like to use, please book an appointment with us. Each structure has distinctly different set-up processes depending on how you intend to operate the business and as such it will be easier to run through these steps with you in an appointment.

SOLE PROPRIETOR

ADVANTAGES	DISADVANTAGES
- 100% Ownership	- Structure must change if other owners are to be introduced
- Complete control over all operations	- Sole traders must raise capital themselves
- You are not responsible for someone else's actions	- Personal assets can be seized to pay for business debts (Unlimited Liability)
- Easy to understand by owner and third parties	- No orderly sequence of ownership or control
- Don't have to register a business name if owner runs it under their own name	- Life of structure limited to life of owner
- Financial results are confidential	- Structure encourages personal goodwill, which can be difficult to sell
- Inexpensive to establish	- High dependency on owner & their health
- Administrative Costs are low	- Does not cope well with high growth
- Owners income not subject to Payroll Tax and Work-cover	- Difficult to control assets pledged to the business (considered a High Risk)
- Profits derived from business is the owners	- Flow of profits to owners cannot be controlled
- Full access to materials, equipment & monies invested in the business	- Subject to marginal tax rates (as high as 48.5%)
- Capital Gains Tax discounts and relief's apply	- Not able to split income to a spouse
- Access to tax free threshold	- Non-commercial loss rules apply to individuals
- No restriction on carry forward losses	- Superannuation contributions not fully deductible
- Rollover available to a company	- No access to Research & Development concessions

PARTNERSHIP

ADVANTAGES	DISADVANTAGES
- Greater access to funding compared to a sole trader	- Technically partnership ends when a partner joins or leaves
- Allows sharing of control	- More people involved in the partnership, less control each partner has (harder to manage)
- Easy to understand by the partners and third parties	- Change in partners can be costly as it is technically a new partnership
- Winding up can be easy depending on the partnership agreement	- All partners personal assets can be seized to pay for business debts (Unlimited Liability)
- Relatively inexpensive to maintain	- Partners are jointly liable for all contracts made by other partners actions
- To some extent, risk is shared	- If no partnership agreement, then profits and losses split equally
- Limited disclosure of financial results	- High risk for partners
- Partners drawings not subject to Payroll Tax or Work-cover	- Unable to accumulate income
- Can cope with any size business provided partnership agreement has required sophistication	- Profit goes to partners, the individuals who are then subject to marginal tax rates (as high as 48.5%)
- Sharing of profits can be varied by agreement	- Splitting of income is limited
- Relatively easy to increase or decrease funds contributed by a partner	- No access to Research & Development concessions
- Tax losses are available for use by individual partners	- Superannuation contributions not fully tax deductible
- Some Capital Gains Tax concessions apply	- Non-commercial loss rules can apply to partners that are individuals
- Ability to split income	- No corporate tax rate unless partner is a company
- Can apply the Simplified Tax System	

COMPANY	
ADVANTAGES	DISADVANTAGES
- Clearly defines ownership & control	- Reductions in capital relatively complex
- Facilitates additional equity funding & transfer of ownership	- Changes in ownership subject to value shifting rules
- Constitution allows for control of changes in ownership and restricts how this occurs	- Owners cannot exercise day to day control unless they are also directors
- Life of structure can be unlimited	- Subject to statutory regulations
- Retention of earning can assist in obtaining non equity finance	- Companies are relatively expensive to incorporate and operate
- Low stamp duty on transfer of shares	- Costly to Wind-up business
- Control of day to day operations can be delegated by owners	- Most smaller companies are required to be audited
- The concept is easily understood by third parties	- Disclosure of information to public
- Directors assets are not usually seized to repay business debts (unless insolvent trading or not proper conduct of role)	- Requires more formalities
- Copes well with any size business and allows for growth and change of operations	- Owners must rely on the directors to run the business
- Company can accumulate assets & income within the structure	- Specific rules apply to debit loan accounts
- Distribution flexibility is limited and profits are distributed via payment of dividends	- Distributions are generally taxed as dividends
- Flat tax rate of 30%	- Specific rules affect the availability of income and capital losses
- Research & Development concessions are available	- Tax free threshold does not apply
- Some Capital Gains Tax concessions apply	- Limited income splitting

UNIT TRUST	
ADVANTAGES	DISADVANTAGES
- Ownership can be defined by units issued and split	- Often has a limited life
- Relatively easy to increase or reduce funding from unit holders	- Change of trustees can be time consuming
- Control can be clearly separated from ownership of units	Can be difficult to understand and this (combined with the corporate trustee) can make maintenance costs expensive
- Relatively inexpensive to establish (but corporate trustee will make it relatively expensive)	- Trustee can be exposed to high level risk
- Allows control where unrelated parties are involved	- Undistributed taxable profits are taxed at 48.5%
- Relatively easy to transfer units	- Although easy to distribute tax free capital profit, they may be taxed in hands of unit holder
- Changes in control are governed by the Trust deeds	- No flexibility for duration
- Simple to wind-up	- Research & Development concessions are not available
- Non taxable profits can be retained	- Small business discounts are not fully passed through to unit holders
- Share of income can be defined	- Trust loss provisions apply
- 50% general exemption and flows through to unit holders	
- Ability to pass on tax credits	
- Rollover to company available	
<i>This structure can be quite complicated to understand so please feel free to book an appointment if you would like some points explained to you in person.</i>	

DISCRETIONARY TRUST

ADVANTAGES	DISADVANTAGES
- Lack of ownership — benefits risk management	- Ownership not clearly defined
- Control can be differentiated from beneficial ownership	- Does not facilitate funding by owners
- Trust deed governs changes in control	- Ownership cannot be split
- Control can be exercised by an appointer	- Can be difficult to understand and this (combined with the corporate trustee) can make maintenance costs expensive
- Rollover to company available	- Often has limited life
- Relatively inexpensive to establish (but corporate trustee will make it relatively expensive)	- Trustee can be exposed to high level of risk
- Simple to wind-up	- Undistributed taxable profits are taxed at 48.5%
- Legal & beneficial ownership is separated and this allows the structure to be an effective measure for asset protection	- Share of income dependant on exercise of discretion by trustee
- Corporate trustee can limit risk of day to day controllers	- Investment by stakeholders cannot be defined
- Non taxable profits can be retained	- Research & Development concessions are not available
- High level of flexibility of allocation of profits	- Can be difficult to pass test for Capital Gains Tax concessions
- Tax free capital profits can be easily distributed (without adverse tax consequences)	- Trust loss provisions apply
- Capital Gains Tax concessions flow through to unit holders	
- Ability to pass on tax credits	
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