Set up as a sole trader

If you are thinking of going into business for yourself, one of your most important decisions will be choosing the correct legal structure for your business. In today's competitive business environment, your choice of business structure could affect your business' long term success.

The most common structures for small business are:

- Sole trader
- Partnership
- Company
- Trust

Each structure has important differences in relation to tax liability, personal financial liabilities and set up costs. The legal structure that you choose for your business will affect:

- Who legally owns your business.
- The legal responsibilities and rights of the owner/s.
- How effectively your structure will protect you from liabilities and legal actions.
- The types and amount of tax that the owners and the business are liable to pay.
- A number of other business issues such as how regulated your business activities will be.

For specific advice about choosing the best legal structure for your business, we recommend that you consult with your solicitor or accountant before making a decision.

Should I operate my business as a sole trader?

If you are planning to operate your business alone (without any partners including your spouse) and if your business will be relatively "low risk", then a sole trader structure may be right for you.

What is a sole trader?

As the name suggests, sole traders carry on business alone, without the use of a company structure and without partners. A sole trader has complete control of the business, including ownership of all profits, business assets and personal responsibility for all debts.

The sole trader has the choice to trade under his/her own name or under a registered business name. A registered business name has no legal implications other than allowing you to use and trade under that name instead of your own. Please note that registering a business name will not protect you from legal claims against your business. Business names can be applied for and paid at the Office of Fair Trading, Department of Tourism, Fair Trading and Wine Industry Development, SmartLicence and State Development Centres.

As a sole trader, you will be liable for taxation as an individual, which means you will be required to declare income from your business in your personal tax return. You will also normally be required to make Pay As You Go (PAYG) tax payments according to the marginal rate of tax for your annual income. Depending on, among other things, how much your business turns over per year,

you may also be required to register for Goods and Service Tax (GST) and remit GST back to the Australian Taxation Office (ATO).

Advantages

The main advantages of operating as a sole trader include:

- It is the least expensive and the most simple business structure to set up and maintain.
- You have complete control of the management and direction of the business.
- You are entitled to all the business' profits and successes.
- There is little paperwork, minimal statutory provisions and minimal government regulations that govern how you operate your business.
- Your business losses can be offset against any other income you earn.
- It provides scope for greater privacy (ie: you do not have to disclosure your profits to the public like you would if you operated through a company).
- It is relatively easy to disband the business.

Disadvantages

For many of the same reasons as other company structures, being a sole trader also has potential disadvantages:

- While you will enjoy all of the profits of your business, you are also fully liable for all of the debts of the business - which means your other (personal) assets, including your house and car, can be put at risk - for the debts and borrowings of the business.
- You alone are responsible for the business which means you may be limited in how long you can stay away from the business. Holidays may become a luxury you can't afford, simply because nobody else has the skills to run your business while you are away. Similarly, the continued operation of the business can be at risk if you become sick or have an accident.
- You are also required to pay tax on profits at your marginal tax rate which may be higher than the company tax rate (as at 30 June 2006 - 30%).
- You are exposed to PAYG tax which can cause difficulties with your cash flow if you fail to put money aside to pay it.
- There are few tax concessions available to sole traders.
- There is no potential for the sole trader to split their income with a spouse or family member, as in the case of trusts or companies.
- The potential for the business to grow is limited because, in the form of a sole trader, the business cannot expand beyond the individual sole trader.

Further information

Contact the ATO on telephone 13 28 61 or internet site at www.ato.gov.au for further information about tax.

For specific legal and taxation advice, consult with your solicitor and accountant.

The following fact sheets provide further information on these issues:

- Business name registration
- Legal aspects of succession planning
- Tax implications of a sole trader