Most Appropriate Business Structure

We often get asked, what is the best business structure? The truth is there is no one size fits all, the answer is which structure is the best for your circumstances, objectives and current financial position.

We choose different structures for different reasons, taxation benefit, risk protection and succession to name a few. Satisfying your objectives is often the hardest as the best structure for risk protection generally is not the best for taxation benefit.

When considering the most appropriate structure, for the optimum taxation benefit and risk protection, there are a number of considerations to take in to account, namely:

- Is the asset/business to be a long term hold or is the asset expected to be sold in the future?
- The level of debt, if any, and the impact of negative gearing on future taxable income;
- The level of exposure to risk, including trading, non-trading, debt levels and staff.

When we consider the most appropriate structure we have three basic options to consider, obviously the first is the simplest, cheapest and easiest for financing purposes;

1. Individual names (includes Partnerships)
2. Company
3. Trusts

The answer to the questions above may impact on the most appropriate structure as will consideration for the top four forms of Australian taxation listed below:

1. Income taxation -
2. Capital Gains taxation — (CGT)
3. Land Tax — (if real estate investment is involved)
4. Goods and Services Tax (GST)

Structures also vary for residents and non-residents, i.e. for non-residents generically we would recommend the most appropriate structure for a property purchase to be a company as trustee for a discretionary trust and a second company to receive the distributions from the trust, if selling the property is a consideration at which time capital gains taxation would be applicable. This option also gives the greatest benefit and flexibility for changing future circumstances whilst minimising income tax liability. However if we are considering a trading enterprise or other risk protection, then different considerations apply. Generally if risk protection is the key objective and asset isolation is the aim a stand-alone company would be the ideal asset holding option, and cheapest alternative.

The current costs for establishing the various structures, including applying for and registering taxation file numbers, goods and services taxation and an Australian Business number, are as follows:

- Individual names - Nil
- Company - $1,848.00
- Company and Trust - $2,583.00

If the proposed generic structure above, with two companies, was the most appropriate the collective cost would be $3,213.00. If specific taxation or other advice is required further fees may apply.

We anticipate, based on current rates, the ongoing compliance costs for preparing and lodging the relevant taxation returns to for the different structures to be:

- In individual name, will depend on other activity in the individuals name;
- $1,500 for one company tax return;
- $2,200 for one company and trust tax returns.

Please see attached for additional information on the different structures.

Business Structures

Sole trader

Last Updated: **30 June 2016**
A sole trader business structure is a person trading as the individual legally responsible for all aspects of the business. This includes any debts and losses, which can't be shared with others. This is the simplest, and relatively inexpensive business structure that you can choose when starting a business in Australia. As a sole trader, you'll generally make all the decisions about starting and running your business, although you can employ people to help you.

Key aspects of a sole trader structure

- Is simple to set up and operate;
- Gives you full control of your assets and business decisions;
- Requires fewer reporting requirements and is generally a low-cost structure;
- Allows you to use your individual Tax File Number (TFN) to lodge tax returns;
- Has unlimited liability - all your personal assets are at risk if things go wrong. Your assets can be seized to recover a debt;
- Any losses incurred by your business activities may be offset against other income earned (such as your investment income or wages). Subject to certain conditions;
- Doesn't require a separate business bank account, unlike a company structure. You can use your personal bank account but must keep financial records for at least 5 years;
- As the business owner, you're not considered an 'employee' of the business. You should pay yourself, which is usually a distribution of your profit, but this is not considered 'wages' for tax purposes;
- If you're a business owner without employees, there's no obligation to pay payroll tax, superannuation contributions or workers' compensation insurance on income you draw from the business. You can currently choose to make voluntary superannuation contributions to yourself though, to help you build up your superannuation, legislative changes from 01/07/2017 will vary this;
- You can employ people to help you run your business. There are compulsory obligations that you must comply with, such as workers' compensation insurance and superannuation contributions;
- It's relatively easy to change your business structure if the business grows, or if you wish to wind things up and close your business;
- You can't split business profits or losses made with family members and you're personally liable to pay tax on all the income derived.
- You must be registered for GST if the annual income turnover is $75,000 or more.

Partnership

Last Updated: **25 January 2017**

A partnership is a business structure that involves a number of people who carry on a business together. You may choose a partnership over a sole trader structure for example, if you'll be jointly running the business with another person or a number of people (up to 20). There are two types of partnerships - general and limited. Partnerships are governed by the relevant law depending on your state or territory:

- ACT - Partnership Act 1963
- NSW - Partnership Act 1892
- NT - Partnership Act 1997
- QLD - Partnership Act 1891
- SA - Partnership Act 1891
- TAS - Partnership Act 1891
- VIC - Partnership Act 1958
- WA - Partnership Act 1895

Key aspects of a partnership structure

- Partnerships can be made up of individuals/companies/trusts or any combination thereof;
- It's relatively easy and inexpensive to set up;
- It requires a separate Tax File Number (TFN);
- If you are carrying on an enterprise, you must apply for an Australian Business Number (ABN);
- It's not a separate legal entity - like a sole trader, you and your business partners are personally liable for the debts of the business;
- You have shared control and management of the business with your partners;
- The partnerships doesn't pay income tax on the income earned. You and each of your partners pay tax on the share of the net partnership income you are each entitled to;
- Requires a partnership tax return to be lodged with the Australian Taxation Office (ATO) each year;
- Each partner is responsible for their own superannuation arrangements - partners are not employees of the partnership;
- You must be registered for GST if the annual income turnover is $75,000 or more;
- A decision made by a partner will be binding on the partnership. Partners are joint & severally liable for partnership liabilities.

Company

Last Updated: **9 May 2016**

A company is a type of business structure. You may consider a company structure when starting or growing your business.

A company is a separate legal entity, unlike a sole trader, partnership or a trust structure. This means the company has the same rights as a natural person and can form contracts, incur debt, sue and be sued. The company's owners (the shareholders) can limit their personal liability and are generally not liable for company debts above that of any unpaid amounts on their share purchases.

A company is a complex business structure, with higher set-up and administrative costs because of additional reporting requirements.

You need to register a company with the Australian Securities and Investments Commission (ASIC). Company officers and directors must comply with legal obligations under the *Corporations Act 2001*.

Key aspects of a company structure

- Is a separate legal entity;
- Has limited liability compared to other structures;
- Is a more complex business structure to start and run;
- Involves higher set up and running costs than other structures;
- Requires you to understand and comply with all obligations under the *Corporations Act 2001*;
- Means that business operations are controlled by directors and owned by the shareholders;
- Must be registered for goods and services tax (GST) if the annual GST turnover is $75,000 or more. The registration threshold for non-profit organisations is $150,000;
- Means the money the business earns belongs to the company;
- Requires an annual company tax return to be lodged with the ATO;
- Net profits are distributed to the shareholders on a franked basis after the company has paid tax on its profit.

Directors Responsibilities

Small business owners need to understand what being a director of a small business company entails. To help small businesses, the Australian Securities and Investments Commission (ASIC) has developed a guide setting out the role and responsibilities of company directors. The guide is particularly useful for small businesses seeking to change from a sole trader to a company business structure.

The guide, entitled *ASIC's guide for small business directors*, provides an overview of directors' duties under the *Corporations Act 2001* and covers the following topics:

- What it means to be a company director;
- How to become a company director;
- Directors' key responsibilities;
- Directors' liabilities when things go wrong; and
- How to resign as a director.

Key points from the guide

- **A director of a company is a person who is responsible for managing the company's business activities.** Even small companies must have at least one director. Larger companies may have many directors who collectively manage the business of the company. They are often referred to as a "board of directors".
- **Shadow directors can still be liable for breaches of the laws relating to directors' duties, even though they were never formally appointed as a director of the company**. Under some circumstances even if you are not formally appointed as a director, you may still be subject to the same duties and liabilities as a director. If you act as a director or give instructions to the appointed directors on how they should act, you may be considered a "shadow director".
- **As a director, you are responsible for the management of the affairs of the company**. You must comply with your legal obligations as a director under the *Corporations Act 2001*. This is the case even if you appoint an agent to look after your company's affairs.
- **Under some circumstances, directors who breach the law can become personally liable for the company's debts and/or be the subject of other regulatory action taken against them**. Once a company is registered, its separate legal status, property, rights and liabilities continue until ASIC deregisters the company. Your obligations as a director may continue even after the company has ceased trading and has been deregistered. Under certain circumstances, as a director you may be personally liable for the company's debts and other losses.
- **Before becoming a director, you should fully understand your role and legal obligations regarding the management of the company**. If you are already a director, or are about to become a director, of a company that has employees, you should immediately find out if the company has any pay as you go (PAYG) withholding or superannuation guarantee charge (SGC) amounts owing to the ATO. If the company fails to meet a PAYG withholding requirement or an SGC liability by the due date, under the ATO's director penalty regime you may become personally liable for a penalty equal to the unpaid amount.

Trust

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A trust is an obligation imposed on a person - a trustee - to hold property or assets (such as business assets) for the benefit of others, known as beneficiaries.

Key aspects of a Trust

- Can be expensive to set-up and operate;
- Require a formal trust deed that outlines how the trust operates;
- Require the trustee to undertake formal yearly administrative tasks;
- If you operate your business as a trust, the trustee is legally responsible for its operations. A trustee of a trust can be a company, providing some asset protection;
- Profits are distributed to the beneficiary pre-tax, with taxation then paid by the recipient.

Knowing the main features of a trust business structure may help you decide if this structure is best for your business, it is important to note there are two types of trusts, discretionary and fixed or unit trusts.

Discretionary trusts are most common as they provide greater flexibility, allowing the trustee discretion to distribute profits annually how they choose to take advantage of each beneficiary's personal taxation position that year. Unit or fixed trusts distribute in a similar way to a company, i.e. according to the number of units held in the trust. Discretionary trusts are also often utilised for asset holding and risk protection as they do provide additional flexibility when the asset is eventually sold.