

# Choosing your business structure: Sole Trader or Company?

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There are four commonly used business structures in Australia:

- Sole trader
- Partnership
- Company
- Trust

**Partnerships and Trusts will be discussed in another article.**

It's important to understand the responsibilities of each structure because the structure you choose may affect:

- the tax you're liable to pay
- asset protection
- costs.

You're not locked into any structure and you can change the structure as your business changes or grows.

## Difference between a sole trader and a company

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Question	Sole trader	Company
<b><u>What are the set-up steps and costs?</u></b>	Obtaining an <a href="#">Australian Business Number</a> (ABN) – <b>free</b> . <a href="#">Business name registration</a> (if applicable) - - <b>one year (\$37) or three years (\$87)</b> .  <a href="#">Separate business bank accounts</a> (recommended, but not compulsory) – <b>bank fees may apply</b> .	Obtaining an <a href="#">Australian Business Number</a> (ABN) – <b>free</b> . <a href="#">Choose and reserve a company name</a> – <b>from \$51</b> (price depends on type of application, reserving a company name is not compulsory). <a href="#">Company registration</a> - <b>\$506 for a proprietary limited company</b> . <a href="#">Business name registration</a> (if applicable) - <b>one year (\$37) or three years (\$87)</b> .

**How is tax calculated?**

Sole traders are taxed as an Individual.

Report your business income in your **individual tax return**.

The 2019-20 **tax-free threshold is \$18,200**.

The amount of tax you pay will vary depending on factors such as your income and deductions you can claim.

**What is the volume Of paperwork and ongoing costs?**

A sole trader is a simple business structure so it generally has less paperwork and lower ongoing costs.

**Paperwork:**

Business income and expenses go in your individual tax return using a separate business schedule – you do not need to lodge a separate return for your business.

Must keep tax records for at least Five years, either electronically, or on paper.

Must have a separate business bank account – **bank fees may apply**.

Companies are **taxed as a separate entity**.

Report company income in the **company tax return**.

There is **no tax-free threshold** for companies. Tax is paid on every dollar the company earns.

The company tax rate is currently 30%.

As a director, you need to **report any income you earn from the company or other sources** in an income tax return. You may also need to lodge a fringe benefit tax (FBT) return if you receive fringe benefits.

A company is a more complex business structure so it generally has more paperwork and potentially higher ongoing costs.

**Paperwork:**

Company must lodge its own tax return in addition to your individual return, and the returns of any associated trusts.

Must keep financial records for seven years to comply with requirements under the *Corporations Act 2001*.

Must keep tax records for at least five years, either electronically or on paper.

Company is subject to annual review by the Australian Securities and Investments Commission (ASIC).

Obligations and legal requirements include : having a registered officer, principal place of business, regular company meetings – including a written record (minutes) of

resolutions, notifying ASIC of key changes etc.  
A company will continue to exist, even if it has ceased trading, until it is **formally deregistered**.

*Note: The level of complexity changes depending on what kind of company you're setting up.*

#### Ongoing costs:

##### Business name registration

(if applicable) - **one year (\$37) or three years (\$87)**.

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Business name registration (if applicable) - **one year (\$37) or three years (\$87)**.  
Annual review fee - **proprietary company \$273**.

Potential for other fees by ASIC including late lodgement fees.

#### How is business income accessed?

Money you earn is treated as your **individual income**.

You can claim deductions for costs incurred in running your business. You can withdraw money from business bank account (separate business bank accounts are recommended, but not compulsory).

Money earned by the company **belongs to the company**.

A separate business bank account is mandatory for a company.

As a director, the company may pay you wages or directors' fees, but you cannot simply draw money from the company as 'personal drawings' from the company. You may also receive money via shares, dividends or loans.

Private companies that make tax-free distributions to shareholders or in the form of payments, loans or debts forgiven, have to adhere to Division 7A Income Tax Assessment Act 1936 (Division 7A).

#### Who is liable for Business debts?

**You are.** Sole traders are personally liable for financial or tax debts.

There is no division between business assets or personal assets, (including your share of joint assets e.g. house or car).

The company is generally liable for all business debts, however your personal assets can also be at risk if you're a director of a company and the company can't pay its debts.

Assets in your name can be **used to pay business debts**.

As a director you are **personally liable for tax debts** including Super Guarantee contributions and Pay-As-You-Go (AYG) withholding.

Even when you cease as a director, you are liable for the period you were a director.

**Can I employ staff?**

**Yes, you can employ staff** as a sole trader business structure.

You will require worker's Compensation insurance.

Understand your tax and super obligations.

Understand your employee's entitlements.

**Yes, you can employ staff** under the company business structure. The company will require workers' compensation insurance.

Understand your tax and super obligations.

Understand your employee's entitlements.

Directors have a legal responsibility to ensure the company meets its PAYG withholding and SGC obligations.

**Do I have full control over the business?**

**Yes** - as a sole trader business structure you will have full control over the business.

**If you are the only director** then you have full control but certain decisions must still be recorded as resolutions of the company.

**If there is more than one director**, you will not have full control – the internal management of the company will be governed by all the directors and in line with certain rules, for example, the company's constitution or the 'replaceable rules'.

**Disclaimer:**

The information contained in this article was prepared by Eugenia Matthews. It is of a general nature only and does not take the place of comprehensive legal and other advice. For advice specific to your circumstances, you should seek independent legal advice.