

key business drivers

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Business Structure

Having the right foundations in place for your business is critical to ensure you set it up for long-term growth and success. And one of the key foundations of your business is your structure. While there's no one 'best' form of business structure that suits everyone, there's generally a business structure that's just right for you.

A variety of options

There are a range of options when it comes to choosing a business structure. It's worth taking the time to consider the characteristics of each form of business ownership and whether they meet your business and personal needs, before making a decision.

Common Forms of Business Structures

Sole Trader

- Simplest form of business ownership.
- Low cost and quick to setup.
- Maintain control over the business operation and direction.
- No tax or legal separation between the individual and the business.
- If the business operates in a name other than the name of the individual, this trading name is required to be registered with the Australian Business Register.
- A sole trader has the greatest level of flexibility and is a common business structure for many trade/labourer services.

Partnership

- Two or more individuals carrying on business together with a common view to profit.
- Similar to a sole trader.
- Low cost and quick to setup.
- Compliment your own expertise and skills with other business professionals.
- Greater access to working capital.
- Each partner is jointly liable for the liabilities of the business and each other's business actions.
- A common tool to govern the operation of a partnership is a partnership agreement.
- A partnership agreement should be written to avoid business disputes but also how to share the profit.

Company

- Creates a separate legal entity from individuals/owners.
- Trades in its own name.
- Asset protection for the company from legal matters affecting the owners and vice versa.
- This limited liability can preserve the personal assets of the individual shareholder from the debts of the company.
- Taxed differently to individuals.

Things to consider

- **Tax** – the wrong structure for your business can have hefty tax implications, so it's worth seeking expert advice.
- **Liability exposure** – any risks you may be exposed to should be considered in line with the optimal business structure for you. Growing companies naturally become more exposed to risks, so it's worth checking in as your business grows and evolves.
- **Asset protection** – your personal assets have certain levels of protection if you set up under a company structure or trust, rather than as a sole trader or partnership.

Trust

- Creates a separate business entity.
- A trust structure is a complex and flexible vehicle to conduct business through.
- Asset protection.
- Flexibility to share the profit of the business.

Combination

- Takes the best aspects attributable to the above structures and brings them together.
- An example is a company owned by a trust.

Worked examples for deciding structure

To help you consider the right business structure for you, let's have a look at some examples of good structures and strategies.

Example one - Partnership of Family Trusts

Two unrelated families start a new business. They want the flexibility of being able to take advantage of the personal marginal tax rates however also want to protect their family assets from the exposure of operating a business. In this example, they could establish a new Unit Trust. The ownership of this Unit Trust can be held 50/50 by two new Family Trusts. The Unit Trust will operate this new start up business. At the end of each financial year, all profits made by the Unit Trust will be distributed to the two Family Trusts in accordance with the Unit Trust Deed. The Trustee of each Family Trust can then distribute the share of profits to the various family members in accordance with the Family Trust Deed, taking into account the personal tax situation of each family member, thus minimising the tax position for the family. The Trustee has the flexibility of distributing differing amounts of income to each family member each year, so as family circumstances change, so can the distributable amount. This structure also provides a level of asset protection for the accumulated family assets.

Example two – sole trader or company?

Imagine you're starting a business where you're selling a particular product that you've created to the public. It may be food or something that touches the body, such as a moisturiser. You may only have a small amount of sales at first at the local markets with a view to expand if successful.

Most people in this situation would commence business as a sole trader and see how things go, but most do not realise the risks they are taking with their personal assets and with their future. With more and more people diagnosed with allergies and people suing businesses for negligence, the need to keep these types of risks separate from you and your personal affairs through a separate structure, is becoming increasingly important.

The main challenge with setting up a separate structure is cost, through setup, ongoing accounting fees, and a proper insurance policy, but the alternative is participating in a lottery that could lead to the loss of the family home – a lottery you don't want to win.

Things to consider

- **Level of direct control**
– sole traders generally have more control over the running of a business than a partnership or company.
- **Running costs** – consider what your regular outgoings are. Depending on your ongoing costs, some structures will provide a better foundation.
- **Access to working capital**
– it can be easier to access capital if you're structured as a company vs a sole trader.

Example three – family trusts and their benefits

Imagine your business has been setup in a company where the owner is your family trust, a combination. You might be working in the family business but your spouse and children are not. Yes, they could be employed in the business but there are several reasons why this might not be the best outcome. If your family trust owns the shares in the company, you can pay your spouse a gross dividend of \$37,000 via the trust. Your spouse would normally expect to receive a tax refund of over \$7,000 per year, assuming franking credits are available and they have not earned other income elsewhere. So by not paying a wage you will save on workers compensation insurance, compulsory superannuation payments and possibly payroll tax, but the best reason for doing this is for when the business is going through a tough year. In this instance, paying a \$37,000 gross dividend (versus a wage) could lead to a personal tax refund of over \$7,000 and no PAYG withholding tax obligations (usually \$4,000) for the company, creating a cash flow turnaround of over \$11,000 for the group.

Some people might say that \$11,000 per year is not much, but for many growing businesses, this saving could fund the extra order for inventory to keep the wheels moving in the right direction rather than the 'one that got away' due to tight cash flow.

The right structure for your business

There are many things to consider when choosing the right business structure for you. And importantly, choosing the right business structure isn't a set-and-forget activity. As your business grows and evolves over time, you may need to check-in with your structure to ensure you've got the optimal one. Two final points to consider when selecting the business structure that is best for you right now are:

- Dealing with other businesses – will it be easier to do business in your line of work as a sole trader or company?
- Impact on personal life – do you want to work with others in a partnership, the responsibility of running a company, or the independence and flexibility of a sole trader?

Want help with your business structure?

Whether you're starting out, revising your structure to expand or want to protect the wealth you've created to date, a trusted DFK adviser can help you get the right foundations in place. If you're ready to make changes or simply want to discuss your options, call us on

1300 DFK ANZ

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