Sole Trader

What is a Sole Trader?

A person wishes to go into business can simply trade under their own name. They can register a name of business (trading name) in respective states to protect against infringement of trade practices.

Set up Procedure

- Register for ABN.
- Register for GST (if applicable).
- Register a Trading name with state authority (if applicable).
- Register for PAYG (if applicable).

Advantages

- Simple.
- Minimal compliance.
- Lower maintenance cost.
- Capital gains tax discounts.
- Total control of assets.
- No set-up costs- Apart from your business name.

Disadvantages

- No asset protection- individual person is liable.
- The structure has a limited life as on the death of the individual the investment must change hands.
- Taxed at your marginal rates.
- Inflexible tax planning.
- Superannuation contribution based on applicable limits.

Compliance Requirements

- ABN registration- compulsory
- GST registration – depends on turnover over $75,000.
- BAS – monthly, quarterly or yearly.
- Tax Return – Yearly.
- Financial Records – Income and expenditure statements.

General Comments

This type of structure is suited for someone with little or no assets and is starting out in business with little turnover. The income tax is either paid at the end of the year after lodgement of Tax Returns or paid through an Income Activity Statement (IAS) during the year and an adjustment at the end. The Owner takes drawings as opposed to wages from a Company and these drawings constitute profits of the Business.

Public liability insurance and other indemnity insurance is recommended.

Roy A McDonald Pty Ltd
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Partnerships

What is a Partnership?

Two or more people can enter into an agreement either verbally or under contract to enter into a business and share in the risks and profits. Partners are jointly and severally liable for any debts and litigations of the partnership.

Set up Procedure

- Register for separate TFN
- Register for ABN
- Register for GST (if applicable).
- Register trading name with state authority (if applicable).
- Partnership agreement (if applicable).
- Register for PAYG-Withholding (if applicable).

Advantages

- Reasonably simple.
- Minimal compliance.
- Mid-low maintenance costs.
- Income Splitting
- Minimise workers compensation and superannuation.
- Capital gains taxed at the partner's level.

Disadvantages

- No asset protection – partners are jointly and severally personally liable.
- Partnership splits income at the same ratio each year.
- Joint tenant partners cannot dispose of their interest separately.
- Tenant- in common partners does not have any right of survivorship.

Compliance Requirements

- ABN registration
- Tax File Number application.
- GST registration – depends on turnover. The threshold is $75,000.
- BAS – monthly, quarterly or yearly
- Tax Return – Yearly
- Financial records – Balance sheet and profit and loss.

General Comments

This type of structure is suited when two or more people enter into an agreement to run a business or investment which enables the profits to be split for tax planning. The income tax is either paid at the end of the year after lodgement of Tax Returns or paid through an Income Activity Statement (IAS) during the year and an adjustment at the end. The Partners take drawings as opposed to wages from a Company and these drawings constitute profits of the Partnership. However, as each partner is jointly and severally liable for the debts of the partnership, the partners should be mindful of asset protection.

Public liability insurance and other indemnity type insurance is highly recommended.

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Company– Limited by Shares

What is a Company?

A company is separate, legal entity and is administrated by its directors. It is formed by people who own its shares and whose liability is linked to the amount (if any) unpaid on the shares respectively held by them.

Set up Procedures

- Purchase a shelf company or establish a new company.
- Register for ABN.
- Register for GST (if applicable).
- Register for PAYG (if applicable).

Advantages

- Limited Liability
- Ability to dispose of the shares rather than the investment, reducing stamp duty and other costs.
- Corporate tax rate lower than the top individual marginal rate.
- Flexible in distribution of income, with some restrictions in case of Personnel Services Income entities.
- No workers compensation on director's fees or dividends.
- **Imputation** credits can be passed to shareholders.
- Superannuation contributions deductible up to age base limits

Retain earnings in the company effectively limits the tax rates to ≤30%. 26.00% for a company that qualifies as a small business with turnover less than $25 Million.

Disadvantages

- Cost of establishing and maintaining is higher.
- Director's potential liability in case of negligence or insolvent trading
- Compulsory workers compensation on wages drawn. Two lots of insurance paid since most self-employed people require income protection.
- Superannuation contributions are required on wages paid.
- Losses cannot be distributed to shareholders.
- More compliance issues accounting standards and ASIC.
- Capital gains are not concessionally taxed.

Compliance Requirements

- ABN registration
- Tax File Number application.
- GST registration (if applicable).
- BAS – monthly, quarterly or yearly.
- Tax Return – Yearly
- Financial records – financial accounts balance sheet and profit and loss in required format.
- ASIC annual return yearly and other changes in directors' shares holding etc.

General Comments

This structure is a popular structure for people running a Business where there is a requirement for asset protection and tax minimisation. If the company is a Mum/Dad type arrangement and they require both asset protection and tax minimisation we recommend a single director company with assets held by the non-director. Public liability is compulsory. The tax rate is ≤30% which is lower than the top individual marginal rate of 45% plus 2% Medicare levy.

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Limited Partnerships

What is a Limited Partnership?

The Limited Partnership provides the opportunity for a business to benefit from the company rate of tax as well as the CGT position of a trust or individual.

When properly structured, the Limited Partnership can satisfy all the characteristics for an ideal structure:

- Asset protection
- Limited Liability
- Distribution flexibility
- Ability to accumulate income
- Accumulated income subject to company tax rate
- Not subject to Division 7A
- Eligible for CGT concessions

Set Up Procedure

A Limited Partnership is formed under the Partnership (Limited Liability) Act. It is necessary to comply with the legislative requirements and register the Limited Partnership before it is recognised under the Income Tax Assessment Act.

A Limited Partnership consists of a general partner and one or more limited partners.

The General Partner

- Has unlimited liability for the debts of the partnership.
- Should not hold any assets other than its 1% (as recommended) partnership interest in the Limited Partnership.
- Should be a company providing limited liability for the shareholders.
- Undertakes the management and conduct of the partnership operations.

The Limited Partner

- Liability is limited to the limited partner's contribution of capital to the partnership (usually $99.00).
- Does not take any part in the management of the business.
- Has no power to contractually bind the partnership.
- Should be a Discretionary Trust providing the highest level of asset protection and income distribution flexibility for the partnership.
- Should hold the shares in the general partner company, if practicable.

Taxation

Limited Partnerships are taxed in the same way as companies for income tax purposes. A Limited Partnership will lodge a company return making calculations of taxable income in the same way as a company.

Receipt of income by a Limited Partnership is a receipt by the Limited Partnership and not the partners separately. As a Limited Partnership is treated as a company for income tax purposes, the partners are not subject to tax unless a distribution is made by the Limited Partnership to the partners.

Distributions to partners (drawings) are classed as dividends which may be 'franked'.

There are no provisions that deem payments, loans to associates or genuine loans to partners to be dividends as in Division 7A.

Uses and Comments

A Limited Partnership can be used as an operating entity, for professionals (eg. medical practitioners, engineers, architects, accountants) and other commercial partnerships (e.g. real estate agents, service entities, development ventures).

A Limited Partnership provides the advantage of limited liability ordinary partnerships lack.

It is possible to restructure an existing ordinary partnership to a Limited Partnership with minimal taxation and stamp duty costs.

Replace Corporate Beneficiary

When a Limited Partnership is used to replace a corporate beneficiary in a trust, the trust will have great flexibility and asset protection and can avoid the issues associated with Section 109UB in Division 7A.

Protecting Company Reserves

A Limited Partnership can be used to effectively protect, extract and access tax paid and non-tax paid reserve in a company and provides flexibility for distribution purposes.

Other Considerations

Care should be taken with the preparation of accounts for a Limited Partnership. When distributions are made to partners, different taxation legislation applies from that for an ordinary Partnership.

The partnership deed must make allowance for this 'point of difference'.

When properly structured, the Limited Partnership can provide a high level of asset protection, income flexibility and minimise the effect of Division 7A.

Trusts – Discretionary

What is a Trust?

A trust is a fiduciary relationship in which a person or company is the holder of an interest in property but is subject to an equitable obligation to use or keep the property for the benefit of another person or for some commitment object or purpose.

In a discretionary trust, the trustee is able to exercise discretion as to who is or are the beneficiaries to be beneficial and what proportions of the trust fund or trust income they are to receive.

Set up Procedure

- Create by a settlor with a Trust deed. (Discretionary).
- Establish a trustee.
- Register ABN.
- Register for GST (if applicable).
- Register for PAYG (if applicable).

Advantages

- With a corporate trustee – limited liability.
- Asset protection – Assets sheltered within the trust.
- Flexible tax planning with ability to distribute income and profits to family and other entities.
- Distributions from trust do not attract workers compensation and SCG.
- Capital gains tax discounting flow through to beneficiaries.
- Can distribute to a Company utilising the Company tax rate but cumbersome

Disadvantages

- Cost of maintenance.
- Changing legislation. Tax is paid at the beneficiary's level hence losing the >30% Company Rate
- Loses the land tax threshold if it owns property.

Compliance Requirements

- ABN registration.
- Tax File Number registration.
- GST registration (if applicable).
- BAS - monthly or quarterly.
- Tax Return – Yearly
- Financial records – Financial accounts balance sheet and profit and loss statement.

General Comments

Most businesses which use a Discretionary Trust is either after asset protection and require the flexibility of distributing to various different entities to minimise their income and capital gains tax. Typically, when the threshold of all beneficiaries are utilised fully the larger businesses typically run through a Company structure to take advantage of the Company's flat rate of tax.

We usually accumulate assets in a Discretionary Trust and we keep the assets separate from the Trading Company that deals with the clients or customers.

Self-Managed Superannuation Fund

What is a Self-Managed Superannuation Fund (SMSF)?

An SMSF has less than five members, each individual trustee of the fund is a fund member, each member of the fund is a trustee, and no member of the fund is an employee of another member of the fund unless those members are related. The requirement that all members be trustees ensures that each member is fully involved in the decision-making process.

Set up Procedure

- Trust deed.
- Appoint a trustee.
- Elect to become a regulated fund.
- Register for a TFN.
- Register for an ABN.
- Register for GST (if applicable).

Advantages

- Asset protected in Super fund.
- Lower tax rate of 15% on income and contributions.
- Retirement planning – payment of pensions.
- Capital gains tax discounts.
- Imputation credits offset tax liability.
- Control over investments.
- A better vehicle than the traditional Testamentary Trust in respect to Deceased estates.
- Can purchase Business real estate property through a trust (conditions apply).
- Can purchase Residential real estate property through a trust or as tenants in common/joint tenancy (conditions apply).

Disadvantages

- Cost of establishing, maintaining and compliance.
- Trustee responsibilities and duties.
- Audit certificate required.
- Contribution surcharge.
- Funds locked until retirement age.
- Government legislation may change in the future.
- Restriction on type of investments it can hold.

Compliance Requirements

- ABN registration.
- Tax File Number application.
- GST registration (if applicable).
- BAS monthly, quarterly or Yearly (if applicable).
- Tax Return – yearly.
- Financial statements – Balance Sheet, Investment Strategy, Profit and Loss, and members' Investment Accounts.
- Yearly audit by approved Auditor.
- Actuarial Certificate (If applicable)

General Comments

Self-Managed Superannuation Funds are becoming increasingly popular. It provides the members with control over where to invest their retirement savings. It is a particularly good tax planning tool when acquiring Business real estate property and many Business owners use this vehicle to assist in purchasing their own Business premises.

It has the lowest tax rate available and is a great tax planning vehicle whilst maintaining control.

At retirement, the income earned by the Superfund is tax free and the allocated pension paid by the Superfund is taxed concessionally giving tremendous tax planning benefits to the recipients.

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Summary - Table for Appropriate Structure

	Sole Investor	Partnership	Private Company	Unit Trust	Discretionary Trust	Superannuation Fund
Administered by	Individual	Partners	Directors	Trustee	Trustee	Trustee
Responsible to	N/A	Partners	Shareholders	Unit holders	Appointer	Members
Cost to establish and run	Low	Fairly low	Higher	Higher	Higher	Higher
Protection of assets from outside risks/ claims	No	No	Only if owned by discretionary trust	Only if owned by discretionary trust	Yes	Yes
Maximum tax rate	Up to 45% plus Medicare levy	Up to 45% plus Medicare or ≤ 30% if Partner is a Company. 26.00% if qualify as a small business entity.	≤ 30% if profit retained 26.00% if qualify as a small business entity.	Up to 45% or if unit holder is company ≤30% 26.00% if qualify as a small business entity.	Up to 45% or ≤ 30% if able to distribute to a company beneficiary 26.00% if qualify as a small business entity.	15% if a complying fund (45% if non- complying)
Potential for slitting income	No	Between partners	Between shareholders	Between unit holders	Between beneficiaries	No, but reduces members tax
Streaming of income	No	limited	No	Dependent on trust deed	Yes, subject to trust deed	No
Taxable capital gains	Paid by individual	Paid by partners	Paid by company	Paid by unit holder	Paid by beneficiaries	Paid by trustee
Access to CGT discount for assets held greater than 12 months	Yes	Yes	No	Yes	Yes	Yes
Other realised capital profits	Not taxed	Not taxed	Taxed as an unfranked dividend to shareholder	May be taxed as capital gain	Not taxed	15% in a complying
Can losses be distributed?	Yes	Yes	No	No	No	No
Flexibility	Poor	Fairly poor	Fair	Good	Very good	Fairly poor
Admission for new parties	New structure is required	Usually permitted	Usually permitted	Usually permitted	May be difficult for non-family members	Usually permitted
Changing ownership	N/A	Partnership interest	Shares	Units	By appointer	N/a
Interest-free loan to relatives	Not taxed as income	Not taxed as income	May be taxed as deemed dividend	Not taxed as income	Not taxed as income	Not permitted