



Business structures

When starting a new business one of your most important decisions is picking the right structure. Your choice will affect how you run, fund and take income from the business. The options for profit-making businesses are:

- 1 Sole trader
- 2 Partnership
- 3 Limited Liability Partnership
- 4 Limited Liability Company
- 5 Franchise

Your choice is not set in stone – for example, you can start as a sole trader and later establish a limited liability company.

1 Sole trader

If you decide to go it alone, you're in good company! A majority of British businesses – more than two million – are one person enterprises. It is the simplest way to get started, with the advantages that you can make all the decisions, be flexible and take all the profits – after you have paid the taxman.

The main disadvantage is that you are personally liable for any business debts. This can be a problem if your business requires a lot of investment – your home or other assets could be at risk.

The buck will always stop with you. And when you go on holiday or become ill, your business may have to stop operating unless you employ staff or have adequate insurance.

Business opportunities are like buses, there's always another one coming."

Richard Branson

Setting up as a sole trader is straightforward. It involves less red tape than any other structure but you must follow some procedures.

Don't forget to register as self-employed with the Inland Revenue. If you leave it for more than three months after starting you face a £100 fine.

Some types of business - for example, restaurants, hotels, cab drivers, child minders and pet shops - will also need a license or permission from the local authority who may want to check your qualifications or inspect your premises.

If you plan to use a trading name that's different from your personal name, you must display your name and business address on all your stationery and signage. You don't have to register your

business name but you should choose it with care. It shouldn't be the same as or too similar to that used by another business – check the National Business Register. And you mustn't use certain words like registered, international and federation.

Many sole traders work from home. You may be liable to pay business rates unless you can prove that the business area of your house is also used for domestic purposes.

You pay tax on your income minus business expenses and personal allowances. Each year you must complete and return a self-assessment form to the Inland Revenue. Be sure to keep receipts for tax-deductible expenses – for example, equipment and business travel. It is always worthwhile hiring a good accountant. You must also pay National Insurance contributions – a small weekly Class 2 levy plus

tip:

You don't have to be Billy-No-Mates! Get along to business networking events and take plenty of your business cards. Alternatively, join an organisation like BGB to get the help of like-minded business people.

Class 4 contributions, depending on your profits. If your turnover exceeds the threshold (£64,000 in 2007/8) you must register for VAT.

And, if you hire staff, you will need to operate a PAYE system to collect their tax and national insurance.

2 Partnership

“Our success has really been based on partnerships from the very beginning.”
Bill Gates

A business partnership involves two or more people. Partnerships are easy to set up and they have the advantages of collaboration:

- You can share the burden. It can be less stressful and lonely if you have business partners. And it's less of a worry if you get sick.
- Partnerships can draw on a wider set of skills and experience. For example, you might be the technical expert while your partner is brilliant at sales.
- You can often make more effective decisions by getting your heads together and considering more of the angles.
- You can raise more investment funds between you and this can help you expand the business more quickly.

You must also consider the disadvantages:

- In a standard partnership, every partner is fully responsible for all the business debts. So if your 'best friend' and business partner disappears with all the takings, you have to pay all the bills.
- Decision making can be slower.
- You may have big disagreements, for example, about whether to expand or consolidate.
- You may get resentful if you think your partner isn't pulling his weight in the business.

Of course you need to choose your business partners very carefully. How well do you really know them? Do you share similar values? Might they run up large bills? Do you agree about long-term plans for the business and the roles you will play?

You should draw up an agreement or deed of partnership. If you don't, you'll be governed by the Partnership Act 1890 – this became law when Queen Victoria was on the throne! Your solicitor or accountant can help you. These are some of the things you need to write down:

- How much has each partner invested?
- How will profits and losses be shared?
- Who does what?
- How much time will they spend?
- How will you make decisions?
- What happens if a partner wants to leave?

How can you change the rules?

Your partnership is more likely to thrive, and survive any bad times, if everyone knows where they stand. You want to be like Ben and Jerry – the successful ice cream partnership – rather than Tom and Jerry.

Aside from making this agreement, it's as simple to set up a standard partnership, as it is a sole trading business.

Partners are individually responsible for paying tax but a nominated officer must complete and circulate an annual partnership tax return form. This can assist all the partners with their self-assessments.

If your trading name doesn't include the names of the partners, these should appear on your stationery with your principal business address.

tip:

Your partnership can include 'sleeping partners'. They invest and take a share of the profits and don't take part in the running of the business. But make sure this has been agreed beforehand!

3 Limited Liability Partnership

Whether you think that you can, or that you can't, you are usually right.” Henry Ford

This is a half-way house between an ordinary partnership and a limited liability company.

The key difference to an ordinary partnership is the reduced risk for individual partners. Their liability is limited to the amount they have invested and any guarantees they have given to raise finance.

But it is more complicated to set up. You need to register at Companies House and get a Certificate of Incorporation. You must also file annual accounts. You should select two designated partners who are responsible for ensuring that the partnership meets all its legal obligations.

tip:

If you don't have at least two designated partners, everyone is responsible for getting the paperwork in on time.

4 Limited Liability Company

“Entrepreneurs are simply those who understand that there is little difference between obstacle and opportunity and are able to turn both to their advantage.” Niccolo Machiavelli

Limited companies are the second most popular business structure after sole trading. There are around two million registered companies in Britain. Key advantages are:

- Limited risk - each member's liability is limited to the amount they have invested and any guarantees they have given to raise finance.
- Companies have more funding options. They can usually borrow more money. They can seek investment from venture capitalists and 'business angels'. If they go public, they can sell shares on the stock market.
- Companies exist in their own right and carry on even when members resign, retire or die.

Key disadvantages are:

- Lots of red tape – it takes plenty of paperwork to set up a company and keep it going.
- Anyone can look at your accounts.
- It is more complex and expensive to wind up a company than sole trading or a partnership.

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tip:

There can be considerable tax advantages for company directors. Talk to your accountant about this.

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Before a business can set up as a limited company – or become ‘incorporated’ – it must be registered with Companies House. The following documents must be completed:

- **Memorandum of Association.** This states your company’s name, ending with the word ‘limited’. The same controls on names apply as with sole traders and partnerships. You can ensure yours is original by searching the Company Names Index at Companies House and the Trade Mark Register at the Patent Office. The Memorandum also states what the company does, the location of its registered office, the amount of share capital it has and how this is divided between the members.
- **Articles of Association.** These are the rules for running the company. They set out how shares are allocated and how they can be transferred, the powers of directors and the rights of shareholders.
- **Form 10.** This gives the names, addresses and other details for the company directors and secretary and the registered office address.

- **Form 12.** A declaration of compliance with the law that must be signed by a solicitor.

The company must submit annual accounts and pay corporation tax on its profits.

Profits after tax (apart from those retained in the business as working capital) are usually distributed to shareholders as dividends.

Directors are appointed by the shareholders and paid salaries as employees of the company. They are often also themselves shareholders. They are responsible for managing the company.

There are two types of limited company. Private Limited Companies cannot offer shares to the public but can have any number of private shareholders. Public Limited Companies – PLCs – can offer shares to the public to raise funds. The minimum value of the shares must be £50,000. A PLC must have at least two directors (a private company needs only one).



5 Franchise

“We’re not in the hamburger business, we’re in show business.” Ray Croc

To operate a franchise business you buy a license to use the name, products and services of an existing company. McDonald’s (which was built up by Ray Croc) is a classic example. It has restaurants all over the world - all run by people who have bought the franchise.

The main benefit is that you can take advantage of a brand that customers already know. You can also use the company’s management support systems.

A key drawback is that your freedom to manage the business is limited by the terms of the franchise agreement. And you often have to pay a share of the turnover to the franchiser, reducing your profits.



tip:

Always seek professional legal and financial advice before signing a franchise contract.