

The Sole Proprietorship: A Popular Form for Small Businesses

by Bruce A. Love

Businesses come in all shapes and sizes. The structure you choose for your business will have legal and tax ramifications. In Pennsylvania, legal business structures include: sole proprietorships, partnerships, corporations, and hybrid variations of these forms.

The easiest, and least expensive, business form is the sole proprietorship. Because of this, they are also the most popular form, accounting for nearly 75% of all U.S. businesses. Sole proprietorships can have any number of employees and may sell products or services (or both). The only qualification for this form of business is that there be only one owner.

What else does it take to start a sole proprietorship? That depends. Let's assume that your last name is Miller and you wake up one morning and decide to start a lawn care business (hopefully you have done more planning than this). If you name the business Miller's Lawn Care, you are in business.

If you decide you would like a more creative name for your business, you will have to register this "Fictitious Name" with the Pennsylvania Department of State (Corporation Bureau) and list the approved business name in a local newspaper and a legal journal. Your business name is considered "fictitious" if it does not include your last name, or if it includes words that suggest additional owners such as "& Company," or "& Sons."

If you have employees, you will also need to contact the IRS to obtain an Employer Identification Number (EIN), and the Social Security Administration informing them of your status. Depending upon your industry you may also need to obtain certain types of licenses.

Sole proprietorships have several very attractive advantages over some other forms of business. In addition to being easy to start,

sole proprietorships give owners the most flexibility (no one else to answer to), allow owners to retain all profits (after taxes), and are easy to dissolve (when the time comes to close a business).

There are also disadvantages to being a sole proprietorship. One of these stem from the fact that there is no legal distinction separating the business from the individual. This can become a major issue if your company ever gets sued. For example, if an employee fails to dilute a powerful lawn treatment chemical prior to spraying a lawn, your business can be sued for any damages caused to the property. If you have no liability insurance, or if damages exceed your insurance limits, the assets of your business will be at risk. If the accident causes personal injury, damages can be very high and the violated homeowner can go after your personal assets if the liquidated assets of your business do not fully compensate the injured party.

Other disadvantages of forming a sole proprietorship include limited ability to raise capital (only one individual's collateral to borrow against), possible management deficiencies (if management is not your forte), and lack of long-term continuity (the death of the owner tends to terminate sole proprietorships).

Businesses can change their structure as they grow and business needs evolve. If you add owners, you can form a partnership. Be aware, however, that partnerships also expose the owners to liability issues. Corporations provide the greatest personal liability protection. To limit liability exposure, consider forming an S-Corporation.

The best option for your business depends upon a variety of factors. Discuss your options with a qualified business advisor, attorney, or CPA.

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