Stephen Larsen and Co
TAX AND BUSINESS ACCOUNTANTS

Guide: Sole trader

There is nothing to stop you commencing business in your own name, e.g. John J Smith.

The sole trader category is a suitable entity for small-scale business operations employing the personal talents of the proprietor.

The owner of the business is personally liable for the debts of the business and all of the owner's personal assets can be utilised to pay business debts.

Limitations

The operational life of the business is limited. When the sole trader dies, the business organisation will come to an end automatically, unless otherwise provided for in a will.

The sole trader's access to finance for establishing and operating the business is more limited than that of a company. It is much easier for a bank or other financiers to obtain a general security over company assets, than to obtain one over a sole trader's business assets.

Taxation

The taxable income of the sole trader takes in the entire taxable income of the business.

There is limited ability to spread income between family members. A sole trader is able to pay a spouse a salary or wage, but must obtain advance approval from Inland Revenue as to the value of the salary or wage.

The sole trader therefore has limited ability to avoid the top marginal individual tax rate, currently 39%.

Assets

The sole trader normally owns the assets of the business in his/her own right.

Liability

The sole trader is personally responsible for any business debt or loss and any business creditor will therefore have the right to claim against the sole trader's personal assets (such as the family home) to enforce a right of payment.

Advantages

However, for a small enterprise, the advantages for a sole trader include:

- Low cost of entry
- Easy to set up
- No significant legal costs
- Only one tax return required
- No registration of name required (if trading under your own name)

Disadvantages

On the other hand, the disadvantages mean:

- You are personally liable for all business debts
- When you die, the business entity dies
- You have limited ability to split income out to other family members
- More limited access to business finance

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