

Title:

Why You Should Never Operate Any Business as a Sole Proprietor

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971

Summary:

All too often new freelancers assume that being independent means being a "sole proprietor." There is no question that operating a sole proprietorship is the easiest, simplest way to start a business. But, no matter what the jurisdiction in which you operate, this is not the way you should operate your business--even just to "get started". Taking any other option, which would involve establishing a legal entity separate from yourself--such as a corporation or limited liability company--is infinitely preferable to operating your business as a sole proprietor.

Keywords:

business success,small business,solo entrepreneur,entrepreneur,start a business,sole proprietorship,partnership,incorporate,corporation,limited liability

Article Body:

One of the primary attractions of being an entrepreneur is being that feeling of being "independent". Defining yourself as an independent entrepreneur does not settle the question, though, of how you should organize and operate your business.

All too often new freelancers assume that being independent means being a "sole proprietor." In the United States, that means that you simply operate your business as your alter ego--you might set up a separate bank account, but you basically operate your business as an extension of yourself. You declare your business earnings on Schedule C of your 1040 and file your business taxes as part of your personal tax return. Other countries have similar systems--in France, for example, translators will more often than not operate as independent members of the "professions liberales".

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separate from yourself--such as a corporation or limited liability company--is infinitely preferable to operating your business as a sole proprietor.

You see, if we were to list the advantages of being a sole proprietor, we would come to the end of the list very quickly. It's simple, yes. It's less expensive, right? Well, no. In fact, the ease of being a sole proprietor gives us our first clue as to why we should not be interested in it. Something that is so easy to do is not likely to bear generous rewards. In business, as in life in general, what is worth having generally takes some effort.

In the case of the sole proprietorship, what is apparently cost-free is actually potentially extremely costly. Indeed, some experts have argued that the sole proprietorship is so dangerous that it ought to be outlawed!

I don't believe that this is an exaggeration. If you're starting your own business, you've probably saved up some money to get started. It takes a while to build a client base, and in the early years, the risks of failure are great. If you have not taken the trouble to structure your business properly by setting up a separate legal entity, you risk losing not only the capital you have invested into the business but everything you own personally as well.

I recall that when I was first getting started as a freelance translator, I received a job offer from a translation agency in Paris. When I looked up this agency on the payment practice lists to which I had subscribed, I was shocked to learn that the agency was suing a freelancer, claiming that through his alleged "negligence", the translator had caused the agency to lose a large account. The sum involved was over 20,000 euros.

Now, if this agency were awarded a judgment and the translator were operating his business as a sole proprietor, if he did not have the 20,000 euros in his business bank account, the judgment creditor (the agency) could attach the translator's personal assets, such as his personal savings, his automobile, and even his family's residence to satisfy the judgment!

If the translator had set up his business as a corporation or LLC, his liability would be limited to whatever resources he had in his corporation's or LLC's bank account and the company's other assets. If these corporate assets failed to satisfy the judgment, the agency would be simply out of luck--it could not touch any of the translator's personal assets.

Now, lest you think that this sort of thing will not happen to you, consider the statistics. One out of every four people in the United States is sued, and one out of every five of those lawsuits causes devastating loss. About 2/3 of those

in attendance at a seminar I attended recently raised their hands when asked if they'd been sued. And remember, the incident I mentioned above involved a French agency. This **can** happen to you, and you must have structured your business properly **before** any lawsuit or threat of a lawsuit arises to be protected.

Besides this key feature of asset protection, you will gain many other excellent advantages by setting up your business as a separate legal entity:

1. You will have considerably more tax advantages. For example, as a sole proprietor you can deduct only 25% of the premiums you pay for health insurance; but your corporation can deduct 100% of such costs.
2. You will be able to split income. If you have a C corporation, you could arrange to receive income through several different entities and reduce your tax liability to the lowest tax bracket.
3. You will be able to use your entity to establish a retirement plan for yourself and your employees.
4. You may be able to reduce social security tax (FICA) liability significantly.
5. If you do business exclusively with clients outside your home state, you could benefit additionally by setting up a Nevada corporation. Nevada not only has no state income tax on corporate profits, it also offers added asset protection through enhanced privacy to both U.S. citizens and non-U.S. residents.

"But isn't it complicated and expensive to set up a corporation?" I am often asked. The short answer to this question is "No." You can set up a corporation with you yourself as the directors and officers. And with all the resources we have available through the web, it has never been easier and more economical to get your corporation or LLC set up correctly.

So don't double and triple your risk and long term costs needlessly. Just don't do it! Get the information you need to get your business set up correctly today.

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