INTELLECTUAL PROPERTY AND TRANSACTIONAL LAW CLINIC

UNIVERSITY OF RICHMOND

SOLE PROPRIETORSHIPS

INTRODUCTORY OVERVIEW

A sole proprietorship is a business owned and managed by a single individual. It is the most common and simplest type of business entity. A sole proprietorship can have multiple people operating the business, but it must have one sole owner.

Sole proprietorships have several advantages over other business entities. They are easy to form, and the owners enjoy sole control of the business profits. However, they also have disadvantages, the biggest of which being that the owner is personally liable for all business losses and liabilities.

With minimal licenses to obtain or separate forms to follow, sole proprietorships are relatively easy to form, easy to maintain, and easy to dissolve.

HOW A SOLE PROPRIETORSHIP IS FORMED

There is no separate cost to establish a sole proprietorship. A sole proprietorship is established when an owner begins operating his business. There are no separate licenses to obtain to form a sole proprietorship. The sole proprietorship will be maintained so long as the owner keeps doing business.

ADVANTAGES OF SOLE PROPRIETORSHIPS

Sole proprietorships have functional and tax advantages compared to other business entities.

One of the functional advantages of sole proprietorships is that they are easier to set up than other business entities. A person becomes a sole proprietor simply by running a business.

Another functional advantage of a sole proprietorship is that the owner maintains 100% control and ownership of the business. By definition, a sole proprietorship can have only one owner, and that owner is entitled to the profits and control of the business.

Sole proprietorships also have tax advantages over other business entities. Under Virginia income tax law, sole proprietorships do not require separate tax filings. Instead, an owner reports the net income or net loss from the business on his personal income tax form. In addition to simplicity, this also avoids the owner from incurring "double taxation" on business income, as in a corporation. Double taxation, which other business entities such as corporations may be subject to, means that the business' income is taxed once when the business makes the profit (the business is taxed), and again when that profit is paid to the owners (the owner is taxed). In a sole proprietorship, the owner is only taxed once, because business profits are filed only on his personal income tax form.

Disadvantages of Sole Proprietorships

Sole Proprietorships also have liability and functional disadvantages compared to other business entities.

The biggest disadvantage of a sole proprietorship is the potential exposure to liability. In a sole proprietorship, the owner is *personally* liable for any debts or obligations of the business. This means that lawsuit claimants or creditors may have access to the owner's personal accounts, assets, or property if any business accounts cannot cover his debt.

While the limitation on ownership can be a functional advantage for an owner, it can also be a disadvantage. If an owner of a sole proprietorship wishes to include another owner, he must dissolve the sole proprietorship and form a new business entity such as a general partnership. There is one exception to this otherwise firm rule – an owner can be a "co-sole proprietor" with his spouse.

Demise of A Sole Proprietorship

A sole proprietorship is dissolved when the owner stops doing business. This can occur if the owner sells the business, passes away and leaves the business to his heirs, or simply closes the business.