



Sole Proprietorship Makes Sense for Startups

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One of the first considerations for the owner of a new business is what form that business should take. The most common options are sole proprietorship, partnership (general and limited), corporation (C corporation and S corporation) and limited liability company.

Most businesses begin as a sole proprietorship, which makes sense for the startup and new business owner. Many sole proprietorships consist of a single individual working at home, developing a product in the garage or writing software code on the home computer. These businesses have few assets other than the equipment and tools used — and usually owned — by the individual. Any assets acquired by the sole proprietor are purchased in the owner's name, although some sole proprietors use a "doing business as" or "d/b/a" name following their own names.

In a sole proprietorship, the business does not exist apart from its owner. All of the profits, losses and deductions for the business are reported on the owner's personal tax return, and the owner of the business is personally liable for all of the business's debts, obligations and liabilities, regardless of whether the owner is using a trade name as a "d.b.a." No regulatory filings are required to establish or create a sole proprietorship, but entrepreneurs should check with local and state tax authorities to ensure the business is in compliance with local and state tax laws.

For most business owners and entrepreneurs, the sole proprietorship will only suit the business and its goals for a limited time. At some point, the business will expand and the owner will be looking for ways to limit his or her personal liability, bring in new partners and seek outside investment. At this point, the business owner needs to consider how — and in what form — to move forward. These are the kinds of questions legal counsel will ask a business owner who is trying to decide whether to become a partnership, corporation or LLC:

- What is the expected or planned growth of the business in the next year? The next three years? The next five years?
- Does the business plan to hire employees or consultants? Will the business pay the employees or consultants in cash or in equity?
- What are the business's financing requirements in the next year? The next three years? The next five years?
- Where will the business have offices? Will they be in state, out of state or both?

- What material contracts does the business anticipate entering into in the next year? The next three years? The next five years?

The answers to these questions will determine what entity is best for the sole proprietor to assume in order to build the business and to meet its evolving goals.

Finance New Mexico is an initiative of the New Mexico Small Business Investment Corporation (NMSBIC) and its partners to assist individuals and businesses in obtaining skills and funding-resources for their business or idea. To learn more, go to www.FinanceNewMexico.org.

