



**BUSINESS STRUCTURES IN AUSTRALIA**  
**(A General Introduction)**

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# **Business Structures in Australia**

## **(A General Introduction)**

### **1. Introduction**

This paper presents an overview of the various types of business structures available in Australia – each of which necessarily attract differing legal and taxation consequences.

### **2. Sole Trader**

Where a person conducts business as an individual, he or she is a sole trader. From a legal point of view there is no difference between the person and the business. As such, the liabilities of the business are the liabilities of the individual – he or she is personally liable for any and all business-related obligations, such as debts resulting from the purchase of goods or services or from court judgments and for the performance of warranty obligations in respect of goods supplied. It is possible for a sole trader to carry on business under a name other than his or her own name. In that case, the name must be registered as a business name under the business names legislation in the relevant state(s) and/or territory(ies).

### **3. Partnerships**

1.0. A partnership is where two or more individuals, corporate or other entities, agree to carry on business together with a view to profit. All partners in the partnership must have the same goals, and each partner is equally responsible for decisions made by the other partner or partners on behalf of the business. All the partners in a partnership are treated equally from a legal point of view. If there is no written agreement, all partners will share in the profits equally, are liable to cover losses equally and are equally responsible for the business' activities and trading. A partnership agreement between the partners should record the term of the partnership and specify all relevant aspects of the partnership.

2.0. A partnership has no separate legal existence from the partners who make up the partnership. So far as third parties are concerned, the liability of the partners for all business debts and obligations is joint and several and unlimited. Accordingly, each partner can be sued, and be required to pay the full amount of any debts of the partnership. If this happens, a partner's only recourse may be to sue or cross-claim against the other partner or partners for their share of the debt.

1.1. A limited partnership is one in which only the general partner conducts the business and has personal liability, while the limited partners, who are basically passive investors, are liable for no more than their stake in the partnership. Forming a limited partnership is possible in some but not all states in Australia.

### **4. Companies**

1.0. A company exists as a legal entity separate from its owners (the “shareholders”) and those who manage the affairs of the company (the “directors”). This means that the shareholders and directors are generally not liable for the debts of the company. Exceptions to the general principle that directors are not personally liable for debts of the company are to be found in provisions relating to insolvent trading as defined in the Corporations Act. In essence, insolvent trading involves incurring a debt at a time when there are reasonable grounds for believing that the company is no longer able, or is likely to be no longer able to pay its debts as and when they fall due.

2.0. The Australian Securities and Investment Commission (“ASIC”) is the regulatory body governing companies in Australia and administering the Corporations Act 2001. ASIC’s aims are, among other things, to provide protection for consumers and businesses in their dealings with companies and to ensure that companies:

1.0.0. operate according to law;

2.0.0. report their activities; and

3.0.0. maintain proper records.

ASIC is also responsible for maintaining an information database containing details of all companies in Australia.

3.0. Most companies fall into two categories, depending on the type of liability that can be imposed on the shareholders. They are either:

1.1.1. companies limited by shares: limits the liability of shareholders to the value of their shares. This structure is suitable for most businesses or trading enterprises. A company limited by shares can be either a private company or a public company; or

1.1.2. companies limited by guarantee: most often used by non-trading organizations such as sporting clubs and charitable organisations.

4.0. **Companies Limited by Shares**

1.1.3. Public Company

This is a company whose shares are owned by the public at large. It is also called a “publicly held” company. A public company must have at least one member (shareholder) but there is no maximum limit on the number of shareholders. There is also no limit on the ability of a public company to borrow funds from the public. The liability of shareholders in a public company is limited to the balance, if any, owing on their shares. A public company has the word “Limited” (or “Ltd”) after its name.

1.1.4. Private Company (or Proprietary Company)

This is a company which does not sell its shares to the general public (e.g. through a stock exchange). The transfer (sale) of shares in such a company is usually restricted in some way, such as by the requirement that the directors of the company must approve any transfer of shares and that new shareholders become members of the company only on registration of the transfer of the shares to them by the company. A proprietary limited company must have a minimum of one member (shareholder) and can have up to 50 members (shareholders). The liability of the shareholders of the company is limited to the uncalled amount, if any, owing on their shares. A private company has the words “Pty Limited” or “Pty Ltd” after its name. The accounting requirements imposed on a proprietary company depend on whether the company is classified a small or a large company. A company’s classification can change from one financial year to another as its circumstances change.

1.1.4.1. Small Proprietary Company

A proprietary company is a small proprietary company for a financial year if it satisfies at least 2 of the following tests:

- 1.0.0.0.0. the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is less than \$25 million; and/or
- 2.0.0.0.0. the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is less than \$12.5 million; and/or
- 3.0.0.0.0. the company and the entities it controls (if any) has fewer than 50 employees at the end of the financial year.

A small proprietary company is only required to prepare an annual financial report (an annual profit and loss statement, a balance sheet and a statement of cash flows) and a directors' report (about the company's operations, dividends paid or recommended, options issued etc.) if:

- 4.0.0.0.0. the shareholders with at least 5% of the votes in the company direct it to do so; or
- 5.0.0.0.0. ASIC directs it to do so.

Although the Corporations Act itself may not require a small proprietary company to prepare a financial report except in the circumstances mentioned above, the company may need to prepare annual financial reports for other purposes (e.g. income tax laws).

1.1.4.2. Large Proprietary Company

A proprietary company is a large proprietary company in a particular financial year if it satisfies at least 2 of the following tests:

- 1.0.0.0.0. the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is \$25 million or more; and/or
- 2.0.0.0.0. the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is \$12.5 million or more; and/or
- 3.0.0.0.0. the company and the entities it controls (if any) have 50 or more employees at the end of the financial year.

Large proprietary companies must prepare annual financial reports and a directors' report. Further, the financial report must be audited and provided to the company's shareholders. Large proprietary companies must also lodge the annual financial reports with ASIC unless exempted by ASIC from doing so.

**5.0. Companies Limited by Guarantee**

A company limited by guarantee is one where the liability of its members is limited to the respective amounts that the members undertake to contribute to the property of the company if the company is wound up. Companies limited by guarantee should not trade or carry on a business with a view to profit. They are suitable for non-profit organisations.

**6.0. Companies Limited by Shares and by Guarantee**

A company can be limited both by shares and by guarantee. These types of company are uncommon in Australia.

**7.0. Other Companies**

1.1.5. No Liability

A no liability company can only be formed for mining purposes. It has a share capital but has no contractual right under its constitution to recover calls made on its shares from a shareholder who fails to pay them.

1.1.6. Unlimited Company

An unlimited company means a company with unlimited liability organised like a partnership but with a corporate body; most often used by investment companies.

1.1.7. Foreign Company

A foreign company means a body corporate that is incorporated in an external Territory, i.e.. outside Australia , and is not:

1.0.0.0. a sole corporation; or

2.0.0.0. an exempt public authority; or

3.0.0.0. an unincorporated body that:

1.0.0.0.0. is formed in an external Territory or outside Australia and the external Territories; and

2.0.0.0.0. under the law of its place of formation, may sue or be sued, or may hold property in the name of its secretary or of an officer of the body duly appointed for that purpose; and

3.0.0.0.0. does not have its head office or principal place of business in Australia.

**5. Trusts**

1.0. A trust structure can be employed in a business or for trading purposes. A trust involves the trustee (usually either an individual or corporate entity) holding certain assets in his, her or its own name but for the benefit of a group of persons referred to as “beneficiaries”. The trustee is required to use any property belonging to the trust for the

good or benefit of the beneficiaries, and not for his, her or its own purposes. Trusts are often created because of the flexibility they allow in tax planning and tax minimization. They are also a popular form of business structure because they allow a flexible means of distributing income and assets and because they can provide certain income tax savings by distributing income among tax advantaged beneficiaries.

- 2.0. A trust itself does not pay income tax on profits, provided that the profits of the trust have been fully distributed to the beneficiaries in the relevant financial year. Trusts are relatively simple to form. However, the law of trusts is quite complex and a lack of appreciation of the law or an inadequately drafted trust deed can give rise to problems. Accordingly, any person contemplating the use of a trust as a business structure should seek legal advice.
- 3.0. The two main types of trusts are:
  - 1.0.0. unit trusts; and
  - 2.0.0. discretionary trusts.
- 1.2. In a typical unit trust, beneficiaries own units in the trust, and the trustee must distribute the income to the beneficiaries/unitholders, in accordance with their respective unit holding in the trust. Accordingly, a unitholder in a unit trust, like a shareholder in a company, has a specific entitlement to a share of the income or property of the trust in accordance with his or her unit holding in the trust. The units may have the same or different rights and entitlements (e.g. as to share of income or capital, voting rights and preferential rights to interest or income) between them.
- 1.3. On the other hand, in a discretionary trust, the trustee has the discretion to decide which beneficiaries will receive distributions of both income and capital, and what amount(s) (if any) they will receive between them.
- 6.0. The discretion as to distribution of income and capital should be exercised afresh each financial year. This is an important advantage in tax planning. Subject to the Corporations Act, limited liability may be achieved with discretionary trusts by the use of a corporate trustee. Discretionary trusts are a common choice for family-run businesses.

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