

A photograph of two business professionals in a meeting. One person is pointing at a document while the other holds a pen over it. A laptop is visible in the foreground.

Small Business Insights

The Pros and Cons of a Sole Proprietorship

Provided by: SCS Agency Inc

A sole proprietorship—also known as individual entrepreneurship, a sole tradership or a proprietorship—is a common and relatively simple business structure. With this structure, a single owner manages an unincorporated business, receives its profits (subject to taxes) and is personally responsible for its debts and obligations. Choosing a sole proprietorship offers benefits and drawbacks. Read on for more information.

Pros of a Sole Proprietorship

Structuring a business as a sole proprietorship offers several benefits, such as:

- **Simplicity and low costs**—Compared to other business structures, sole proprietorships are generally easier and less expensive to start. There is typically no need to formally register the business or provide notification of its formation to state or federal offices. Start-up costs may only include business name registration fees and license and permit fees.
- **Full control and flexibility**—Without shareholders or partners, sole proprietors are free to make decisions as they deem appropriate. This structure also offers flexibility to change the business's course quickly.
- **Fewer government regulations**—The government has relatively few regulations over sole proprietorships, and they are not held to the same reporting or disclosure standards as other business structures. For

Sole proprietorships offer several advantages compared to other business structures. However, their disadvantages must also be considered.



example, sole proprietorships are not required to formally register with the state. The lack of regulations can reduce paperwork and grant the owner added privacy and autonomy.

- **Tax simplicity**—Sole proprietors aren't required to file for an employer identification number with the IRS and can use their Social Security number. Additionally, sole proprietorships are pass-through entities, with the business's income and losses reported on the owner's personal tax return.
- **Easier banking**—Although it may be beneficial, setting up a separate business bank account is not required for sole proprietors. This can save time when getting started and make the payment process easier.

Cons of a Sole Proprietorship

While sole proprietorships have advantages, there are also drawbacks to consider, such as:

- **Unlimited personal liability**—Since a sole proprietorship does not establish a separate business entity, owners are personally liable for business activities. This could place personal assets in jeopardy.
- **Difficulty in raising money and securing loans**—Without the ability to sell shares in their business, sole proprietors may have difficulty raising capital. Additionally, lenders may be more hesitant to issue credit to a sole proprietorship than they would to a business structured with limited liability. These factors may inhibit the growth of a sole proprietorship.
- **High self-employment taxes**—Sole proprietors must pay Social Security taxes and Medicare taxes since they are both the employer and the employee. While they may be able to claim some of the amount as a deduction, the taxes may be an unappealing aspect of this structure.
- **Succession difficulty**—Since sole proprietorships are not separate business entities and intangible assets cannot readily pass to another owner, they can be complicated to sell.
- **Reduced collaboration**—Without a board or partners, sole proprietors may have fewer collective brainstorming opportunities, and knowledge or skill gaps that can create weaknesses in the business may exist. Taking time off to train or hire assistants may also reduce potential profits.

Choosing a Sole Proprietorship

Determining if a sole proprietorship is right for a business requires analyzing its pros and cons and comparing alternative business structures. Seeking professional or legal advice may also be beneficial when making such a decision.



Contact us today for more small business insights and risk management guidance.