MODERN MEMBERSHIP

Legal

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CHOSING THE RIGHT BUSINESS STRUCTURE FOR YOUR PROFESSIONAL BODY

Starting a new professional body comes with an amount of uncertainty, but also a lot of excitement. It's easy to get wrapped up in all the little things and the founders often don't take the time to really consider the best structure for their organisation.

Choosing the right format from the start can spare you a lot of headaches later on. Each legal structure has different pros and cons, and factors like the size, nature, and ownership of the new business all has an impact on the decision. Each format has different effects on taxes, personal liability, admin costs, the amount of paperwork, and the ability to raise money.

Business Structure Options?

There are a number of different structures for businesses in South Africa, including:

- Sole Proprietorship: 1 owner
- Partnership: 2-20 owners
- Private Company: 1-50 owners
- Business Trust: No limitation on ownership
- Incorporated Professional Practice: Only available to certain professions, e.g., lawyers, accountants, and doctors
- Non-profit organisation
- Public company: Listed entity with no limit on ownership
- State-owned company
- Close Corporation: This form was discontinued, and no new registrations were allowed after 2011, although existing Close Corporations still remain.

Non-profit company

A non-profit company is incorporated in terms of the Companies Act for a broader public purpose, for example some form of cultural or social activities or communal / group interests. Income from this type of business structure is not distributed to any director or incorporator but is used to further the objectives of the NPC.

Under the previous Companies Act of 1973, these companies were known as Section 21 companies or companies limited with guarantee. Non-profit companies are now dealt with in Schedule 1 to the Companies Act.

The income and property of a non-profit company are to be applied solely for the promotion of the non-profit company's objectives. Non-profit companies are generally not taxed on income related to their objectives due to the benefits they contribute to society. These companies must register separately under Section 30 of the Income Tax Act to receive additional benefits as a Public Benefit Organisation (PBO).

The most common for-profit structures for small businesses include sole proprietorship, partnership, and private company.

Sole Proprietorship

A sole proprietor, also called a sole trader, is a person who trades in his or her own name. It's the simplest form of business, and there is no need to have a business name or to register the entity (although you will have to register with SARS for all applicable taxes).

Advantages:

- Setting up a sole proprietorship is cheap, especially if you have no employees.

Disadvantages:

- The sole trader is personally liable for all debts. If the business fails, you can lose all personal assets.
- Can have only one owner.
- Raising funds can be cumbersome.

A sole proprietorship is a typical choice for a small business where the owner expects a lower turnover, intends to work alone, and funding requirements are low, for example, a service provider.

Partnership

A partnership is similar to a sole proprietorship, but with more than one owner. It has similar benefits and drawbacks with a few additional disadvantages.

Advantages:

- Setting up a partnership is cheap, especially if you have no employees.

Disadvantages:

- The partners are personally liable for all debts. If the business fails, creditors can seize the personal assets of individual partners.
- Raising funds can be difficult.
- Every time a partner retires, or a new partner is introduced, the old partnership comes to an end, and a new one is formed.
- Administration and tax can become complex, especially when there are changes in the partnership.

Private Company

A private company is a separate entity that is registered with the Companies and Intellectual Property Commission (CIPC). The company has both shareholders and directors, which can be the same or different individuals.

Advantages:

- A company is a separate entity, which means the debts belong to the company and owners have limited personal liability when the company can't pay its bills.
- A company appears more professional and may attract more clients of a higher caliber.
- More than one owner is allowed.
- Selling portions or shares in the business is easy.
- It is usually simpler to raise funding. Apart from applying for loans, companies can also issue shares or debentures.
- There is more flexibility in setting up favourable tax structures. Small businesses may apply for the Small Business Corporation tax rates, which are much lower than standard company tax rates.

Disadvantages:

- Administration and set-up costs, which are more expensive, includes an annual fee payable to CIPC.
- Private companies may need to be independently reviewed or audited.

A private company is usually a good business structure choice for a complicated or risky business, when a higher turnover is expected, long-term growth is anticipated, and more employees will be appointed.

Considerations Influencing the Choice of Business Structures

There is no one-size-fits-all and no structure that is inherently superior to another. There are different factors to consider when choosing the best structure for your professional body. These include:

- **Financing needs:** A sole proprietor and partnership have limited access to funding, which usually includes only loans. A company has more choices and can sell shares to raise additional financing.
- **Admin costs:** A company has more admin costs compared to that of a sole trader or partnership.
- **Tax considerations:** Different structures have different tax implications. These are often complicated and require the help of an experienced accountant.
- **Business continuity:** If one of the owners leaves a company, it can continue trading. In a partnership, the structure dissolves when someone leaves, and a new partnership needs to be set up.
- **Selling of business:** A sole trader can only sell its assets, while a company can sell the whole entity.
- **Insolvency:** If a sole proprietorship or partnership becomes insolvent, creditors will be able to seize personal assets. A company, on the other hand, owns its own assets and debts, which means that personal assets cannot be touched. Exceptions to this include a shareholder signing personal security for a debt, the directors being involved in reckless trading, and Incorporated Professional Practices.
- **Flexibility:** A company provides more tax and ownership flexibility.
- **Future needs:** How will the professional body look in five to 10 years? Are there plans for growth? What happens if a partner passes away or leaves the business? What if the organisation is unsuccessful?

How to Choose the Right Business Structure

Choosing the right business structure is an important decision, and you need to understand the benefits and downsides of the different options. Get it right from the outset – choosing the wrong structure or changing to another structure later can be costly.

At E2 Solutions, when we advise our clients, we first gain a thorough understanding of their intention for the professional body and take all factors and their future needs into account. This way, we get a high-level picture of their current business model and how our software can better enhance this.

What is the most common form a of business structure for a professional body?

An NPO is the most common form of business structure chosen by professional bodies in South Africa.

To find out more about the possibly business structure you should consider, contact michele@e2.co.za