DISCLAIMER

This Guide is an overview only, which is intended to help social entrepreneurs to select the most appropriate legal structure for their social venture. This Guide reflects the law in force in England and Wales as at 1 July 2016. The Guide is general in nature and may not apply to the particular factual or legal circumstances which a social venture faces, and we therefore recommend that independent legal advice is sought. The Guide does not constitute legal advice and should not be relied on as such.
## SOLE TRADER

### AT A GLANCE

### SUMMARY

A sole trader is one person carrying on a business on their own without any separate legal identity.

### ADVANTAGES

- ✓ Easy to start up: no formal set-up is required
- ✓ Very flexible structure: the individual can decide if profits are retained by them or reinvested in the business/social purpose
- ✓ No public reporting requirements: information/accounts are not made publicly available

### DISADVANTAGES

- ✗ No limited liability for the individual: if the business fails, the individual is responsible for the debts and other obligations of the business
- ✗ Risk of losing ‘goodwill’ in business name as the business name is not registered at Companies House
- ✗ Difficult to raise finance: unsuitable for equity finance, and difficult for large loans
- ✗ Other legal structures may be more immediately identifiable as social ventures (such as a CIO, CIC or cooperative and community benefit society) and gain the commercial benefit such identification brings more readily
CASE STUDY

WELL GROUNDED

Well Grounded is a social enterprise established by UnLtd Award Winner, Eve Wagg, which provides unemployed young people with a career in the coffee industry, training them as baristas and finding permanent work within the hospitality industry. Building on the success of a pilot scheme, Well Grounded is rolling out a 12-week Speciality Barista programme in September 2016 to provide more young people with the opportunity to gain a career in one of the fastest growing markets in the world.

Eve initially ran Well Grounded as a sole trader, as she wanted to test the concept and value proposition of the business quickly, in order to identify demand from her target customer base before incorporating.

After the pilot, Eve decided to incorporate Well Grounded as a CIC in January 2016 as she had found that operating as a sole trader was restricting the funding and investment she could obtain.

Eve chose the CIC model as she wanted the legal structure to make the venture’s social impact very explicit, while still developing a commercially viable business. Further, Eve feels that being a CIC provides entry into a wider movement and community that is committed to proving that business can be social.

She considered charity status too, which would have enabled her to access a number of other funding grants and gift aid, but ultimately decided that charity status is not consistent with Well Grounded’s long term business model.
SOLE TRADER

a. OVERVIEW

A sole trader is one person carrying on a business on their own, with complete control over its operations. There is no separate legal entity for the business. A sole trader can employ other people in their business, but generally speaking, sole trader businesses are small in scale, with low turnovers, and few (if any) employees.

Being a sole trader is one of the most straightforward ways to establish a business. It does not require any documents to set up the business, nor payment of any registration fees, and there are no formal requirements for business accounts, so the sole trader can decide how sophisticated these will be (subject to HMRC’s requirement that proper records are maintained and kept for a certain period). All profits generated by the business belong to the sole trader personally.

If choosing at the outset between forming a company and running your business as a sole trader, you will need to carefully weigh (i) the cost of establishing and administering a company and (ii) the benefits inherent in company structures, such as limited liability, which are discussed in section 2.4(c) ‘Liabilities’ in the section relating to private companies limited by guarantee and section 2.5(c) ‘Liabilities’ in the section relating to private companies limited by shares.

b. ESTABLISHMENT COSTS AND DOCUMENTATION

Unlike companies, sole traders do not need to prepare any documents to establish their business, and do not register their business with Companies House. Sole traders can simply start trading or carrying out their business activities immediately.

A sole trader can trade using their own name, or under a business name of their choosing. If a sole trader uses a business name of their choosing, there are restrictions on what names may be used, and requirements as to what information the sole trader must be displayed at its place of business and in correspondence. For further information, visit https://www.gov.uk/choose-company-name.

A disadvantage to non-registration is that sole traders are not able to register their business name with Companies House. Therefore they run the risk that their business name may be registered by another entity. Further, it is not possible to reserve names at Companies House.
It should be noted that in the absence of protection by way of a company name registered at Companies House, a sole trader may wish to consider trade marking or protecting the copyright of any names/logos used in the business. This can, however, be expensive and in these circumstances the sole trader should obtain specific legal advice. For more information on establishing a sole trader business, visit https://www.gov.uk/set-up-sole-trader.

c. LIABILITIES

As a sole trader does not have a separate legal entity for their business, the sole trader does not benefit from limited liability. The sole trader will be personally liable for all of the debts and obligations of their business. This means that a sole trader’s home and other personal assets can be seized to satisfy business debts. This is one of the biggest disadvantages of operating as a sole trader in comparison to corporate forms which offer limited liability, such as a private limited company. Please see section 2.4(c) ‘Liabilities’ in the section relating to private companies limited by guarantee and section 2.5(c) ‘Liabilities’ in the section relating to private companies limited by shares for more information on limited liability.

d. TAX TREATMENT

Sole traders should register with HM Revenue & Customs (‘HMRC’) as soon as possible after starting business. At the latest, sole traders should register by 5 October of the business’s second tax year or face a penalty. As sole traders are self-employed, profits are taxed as personal income and should be included in the sole trader’s personal self-assessment tax return each year. To register for self-assessment, visit https://www.gov.uk/register-for-self-assessment.

Sole traders may be required to register for value added tax (‘VAT’). If taxable supplies made by the sole trader’s business in the previous 12 calendar months exceed the threshold for registration (currently £83,000), then the sole trader must register for VAT. If the sole trader’s taxable supplies are below the threshold, they may nevertheless voluntarily register for VAT.

Sole traders can hire employees, in which case they are responsible for deducting income tax from salaries paid to employees and accounting to HMRC for both employer’s and employee’s national insurance contributions.

Individuals who sell their business may be eligible to claim entrepreneurs’ relief on the disposal proceeds if they sold ‘qualifying assets’, which has the effect of applying a reduced rate of capital gains tax (currently 10%) to the qualifying gains.1 Where a sole trader disposes of the whole or part of their business ‘as a going concern’, that is, all of the business assets are acquired by a third party who intends to use those assets in the continuation of that business, the sole trader may qualify for entrepreneurs’ relief on the capital gains made.2 You should seek further tax advice if you believe you might qualify for the relief.

e. ONGOING GOVERNANCE AND REGULATORY OBLIGATIONS

One of the main advantages of being a sole trader is that the administrative requirements are less burdensome than corporate structures. In particular, the business of the sole trader is not required to file a confirmation statement or annual accounts with Companies House. However, this does not mean that the sole trader does not have to keep any records; the sole trader must ensure that complete and proper records of the income and expenses of the business are kept.

f. CORPORATE STRUCTURE

A sole trader’s business does not have a separate legal personality from the sole trader. In other words, the sole trader is the business. This means that the sole trader is personally liable for the liabilities of the business, as discussed in section 2.1(c) ‘Liabilities’ above. Contracts and applications for loans must be made in the personal name of the sole trader.

g. FINANCE AND FUNDRAISING

Financing opportunities for sole traders are limited. Generally, sole traders raise money for the business out of their own assets and/or through loans from banks or other lenders (often using their personal assets as security or giving personal guarantees). Sole traders may also seek funding from friends and family, normally through small informal loans. Recent years have also seen the successful use of crowdfunding as a means to raise capital

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2. The sole trader must own the business for the period of one year ending with the date of disposal.
for starting a business. Sole traders can raise funds through donations-based and rewards-based crowdfunding. However, as sole traders do not have shares that can be issued to investors in return for cash, equity-based crowdfunding is not an option. Loan-based crowdfunding may be difficult as the obligation to repay a loan is a substantial liability and many lenders will insist on incorporation and may require security for that loan.