Business Structure and Financial Statements

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**Sole Proprietorship**

**Tax-related Advantages and Disadvantages of Sole Proprietorship**

**Advantages**

The advantages of a business organization like Sole Proprietorship are;

1. The financial requirements for starting and running a Sole Proprietorship are much lower than other business organizations, so in this way, the business owner pays lower amounts of taxes on the funds which he/she has for starting or running the business organization.
2. The owners of Sole Proprietorship does not pay any corporate taxes while they are only required personal income tax once they receive the revenues (Masten, 2012).
3. The amount and tax rates are lower for the Sole Proprietor because of the low amount of capital as compared partnership and corporations.

**Disadvantages**

The disadvantages of a business organization like Sole Proprietorship are;

1. In most of the cases, the single handled owned business organization mostly pay taxes personally based on the GAAP principle that business and owner of the business are two separate entities.
2. As the business is of a smaller size than other categories, so the taxes become huge and unaffordable burdens for the business to pay (Masten, 2012).
3. Lack of providing tax benefits to the sole proprietor by the state like health insurance benefits for employees etc.

**Partnership**

**Tax-related Advantages and Disadvantages of Partnership**

**Advantages**

1. Partnership organizations do not pay separate income tax while the partners declare their business income share into their personal tax returns.
2. The partners are considered as one and equal by the IRS (Internal Revenue System), so the tax has been distributed among partners equally that decrease the burden for all individually (Masten, 2012).
3. In partnership, the partners are not required nor do they pay estimated taxes.

**Disadvantages**

1. The problems occur when all partners are considered equal while calculating taxes because all partners do not exercise the same amount of returns/revenues.
2. There is limited liability of partners in partnership which is financial risk for them but they also have to pay higher amount of taxes, so increase the risk level.
3. Partners are required to register themselves with HM Revenues and customs as self-employed, for which they pay an additional tax (Masten, 2012).
4. Tax laws are more complex for partnership organization in comparison with other business organization.

**Corporation**

**Tax-related Advantages and Disadvantages of Corporation**

**Advantages**

1. The tax laws and policies for corporations are very clear and justifiable than sole proprietorship or partnership.
2. The taxation of owners (shareholders) of corporation organizations is always independent.
3. Tax benefits like health insurances for the employees are provided to the corporation by the state.
4. Reasonable compensations are available for the shareholders which benefit then in taxes.

**Disadvantages**

1. Benefits of the corporate business owners (shareholders) are treated as taxable income by thetaxationbodies**.**
2. Double taxation by the owners, one is on the distributed profit among shareholders while another tax payment is done on their personal incomes.
3. The requirements for maintaining tax status of corporations are highly strict and complex as compared to the requirements for sole-proprietorship and partnership (Masten, 2012).
4. Reclassification earning of the corporation is considered as wages that lead higher amount of taxes if shareholders do not get reasonable compensation which not always possible to be gotten.

**Limited Liability Company (LLC)**

**Tax-related Advantages and Disadvantages of LLC**

**Advantages**

1. Tax rates are dependent on the income level of owners so the owners mostly pay taxes at lower tax rates than the corporation.
2. The owners of LLC organization are free from double taxation.
3. In number of states, LLC is not required to pay franchise which is a crucial benefit for this category of the business organization when compared to corporations (Masten, 2012).

**Disadvantages**

1. All revenues of Limited Liability Company are taxable.
2. There is no tax exemption to be exercised on the property of LLC.
3. The owners pay self-employment taxes like partnership.

**Chosen Business Structure when Staring Own Business**

Choosing a business structure when starting a business depends on three basic factors which are Capital & liability, record keeping, and taxation. Being a business student (not a business professional), I would choose the business structure of Sole-Proprietorship. The Sole-Proprietorship business structure will be chosen because it does not need huge amount of funds when starting. As well as Sole-Proprietorship does not require the owner to fulfill high-level requirements as required for starting partnership or corporation(Pettit, & Singer, 2005). Beyond that, this business structure will be preferred to choose because it provides full control of ownership to the single owner where I would be independent in making and taking any business decision.

In addition, the rate of taxes on Sole-Proprietorship are much lower than the tax rates for other business organizations as well as the management and administration of Sole-Proprietorship is too simple and easy in comparison with partnership, corporation or LLC (Limited Liability Company).

**Financial Statements for Sole-Proprietorship**

* **Balance Sheet**

Balance Sheet is one of the most important financial statements. Balance sheet shows the financial position of the business over a specific period of time. In Sole-Proprietorship, balance sheet shows held assets by the business, liabilities and the volume/amount of owner's equity.

* **Statement of Financial Performance**

Statement of financial performance or income statement is the major financial statement for sole-proprietorship that shows the financial performance of the business over a period of time.

**Statement of Changes in Owner’s Equity**

The Statement of changes in Owner's Equity is one of the financial statements that work as the link between the income statement and balance sheet of the business by showing the changes occur in the owners' equity (Pettit, & Singer, 2005).

* **Statement of Cash Flows**

The last financial statement for sole-proprietorship is the statement of cash flows that explains where the cash of business goes or went and from where the cash comes in.

* **Financial Statements and Business Decisions**

In business decision making, all of the financial statement help in different way. The balance sheet helps to know the actual business position in terms of its assets, liabilities and owner's equity. This help in decisions regarding investments or business expansion. Income statement helps in the way to know the financial position of the business so that the owner takes decisions accordingly. Statement of changes in owner's equity helps in a way the business is majorly run by the capital or by the liability (Pettit, & Singer, 2005), while statement of cash flows is helpful and beneficial to know the current assets (cash) of the business so any business decision can be made a successful one.

**References**

Masten, S. E. (2012). A legal basis for the firm. Journal of Law, Economics, & Organization, 4(1), 181-198.

Pettit, R. R., & Singer, R. F. (2005). Small business finance: a research agenda. Financial management, 47-60.