

Flying "Sole" Not Recommended

Why Restaurants Should Never be Sole-Proprietorships

Many of you probably already know that for the simplest tax treatment you should conduct your business as a sole-proprietor. It's easy. As a sole-proprietor you don't have to separate your personal income from the business income, nor do you have to worry about expenses being separated. The business is the individual and the individual is the business.

However, simplest is not always best. Unfortunately, it doesn't work for a restaurant. The reason is clearly based on the liability issues surrounding a restaurant. I'm not going to address the tax treatment differences of a sole-proprietor versus a corporation or an LLC. I'm merely addressing the liability protection you need to seek when the possibility of being sued by someone is as high as it is with a restaurant, especially one that serves alcohol.

First of all, a restaurant owner should incorporate their restaurant either by using a corporation, LLC or LP. Do not use general partnerships for protection as each of the partners is personally liable for the actions of the business. This is a first step in keeping the owner's personal assets from becoming a target of a creditor of the restaurant. An LLC or LP can increase the amount of protection that the restaurant has because of the inability for a creditor to get at the actual assets of the business. Instead a creditor is only entitled to the owner's share of the profits and does not have any say in the management of the company. A single member LLC does not necessarily share that same protection. You should seek the advice of an attorney in setting

up a single-member LLC so that the protection is not diminished or lost.

A restaurant owner that has the building, land and daily operations of the business all in the same entity should also consider moving the bigger assets to a separate entity. For instance, LLC "A" would own the building and land and then LLC "B" would own the daily operations, furniture, fixtures and equipment within the restaurant. This would offer further protection of those assets from lawsuits if the restaurant were to be sued for some reason.

When I said setting up the corporation was the "first line of defense" against possible lawsuits, I was alluding to the fact that many restaurant owners do not conduct their business as a separate entity. This means that the corporate veil can be pierced, and it will be as if there was no protection at all. In order to maintain the protection for all entities, it is necessary to keep funds from co-mingling. If the restaurant needs money, then the owner should put it into the bank then pay the expenses from the business bank account, not pay for the expenses personally. If this occasionally happens, then an expense report can be used to gain repayment, but if it happens on a continuous basis, then the courts could rule that the entity is really an alter ego and

pierce the shield. If the restaurant is a corporation, it is necessary to follow at least these steps to insure that the corporation is acting like a corporation:

- Have regular board of directors' meetings
- Have annual shareholders' meetings
- Issue corporate stock or maintain the stockholders' ledger
- Maintain up-to-date corporate records



By **Tonetta Weaver**
TM Accounting Services, LLC

- Have the initial organizational meeting (should be done at start-up)
- Adopt corporate bylaws
- Maintain proper accounting records
- Advertise and serve notice that the business is operating as a corporation (should be done at start-up)
- Get proper business licenses for state and local agencies
- File annual tax returns

If the corporate shield is pierced, and you have other family members listed as directors or officers, then their personal assets could be at risk. Also, if you make a personal guarantee in order to get a loan, then the protection from that creditor is lost even if you have a corporation, LLC or LP. Remember, in order for the protection to work, the restaurant has to maintain a separation from the owners, managing members, or partners.

Going it "sole" won't protect you if you need it. Take care to set up the proper business model now.

Tonetta Weaver is the founder and owner of Phoenix-based TM Accounting Services, LLC, specializing in accounting services for small businesses. Visit www.tm-accounting.com.

