Lesson 2.

Organizational and legal forms of economic activity

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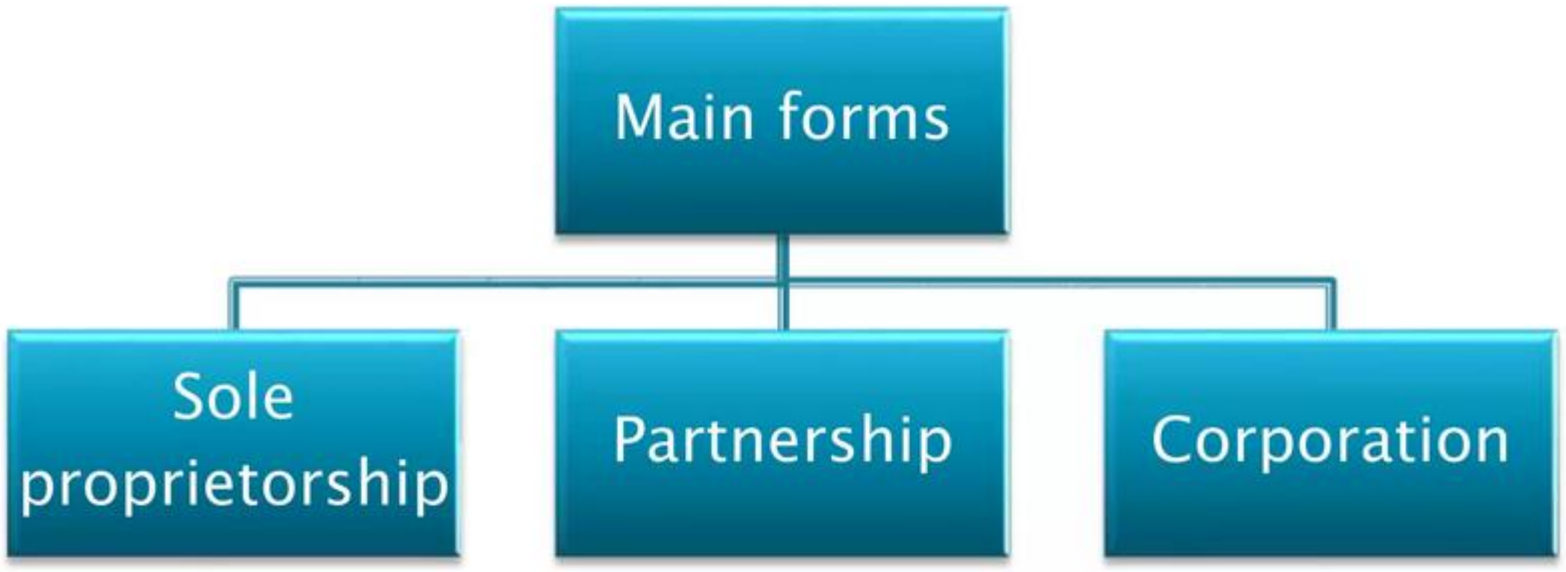
Forms of Business Ownership



Sole Proprietorship

- Definition
  A business that is owned by one person.
- Most common in retailing, service, and agriculture.

SOLE PROPRIETORSHIP

- Owned by one person, who performs most roles and owns everything
- Owner gets all profits, takes all the losses → called **unlimited liability**
- Easiest and least expensive to set up
- Easiest for tax purposes → income recorded under personal income

Sole Proprietorship or Individual Entrepreneur

Advantages	Disadvantages
• Ease of Start-up and Closure • Pride of Ownership • Retention of All Profits • Flexibility of Being Your Own Boss • No Special Taxes	• Unlimited Liability • Lack of Continuity • Lack of Money • Limited Management Skills • Difficulty in Hiring Employees

Partnership

- An unincorporated business structure that **two or more parties** form and **own** together is called a **partnership**. These parties, called partners, may be individuals, corporations, other partnerships, or other legal entities.
- Partners may contribute **capital**, **labor**, **skills**, and **experience** to the business. They may have **unlimited legal liability** for the actions of the partnership and its partners.

PARTNERSHIP

- Two or more individuals share costs and responsibilities
- Terms of partnership recorded in **partnership agreement**
- “silent” partners- partners that usually will front a lot of capital, but do not want to participate in business decisions – receive profits in return

Comparing 3 Types of Partnerships in Business. There are three relatively common partnership types:

1. **General partnership (GP)**
2. **Limited partnership (LP)**
3. **Limited liability partnership (LLP)**

1.General partnership (GP)

General partnerships are the most basic form of partnership and they don't require forming a business entity. This means they're not a separate legal entity, but simply a formal agreement between two or more persons carrying out business together. The partnership agreement clearly outlines the various rights and responsibilities of individual partners. This includes decision-making processes, split of profits and exit procedures:

Features of general partnerships:

- partners evenly split profits and ownership
- partners have independent power to bind the company to loans and contracts
- partners have total liability, meaning they're personally responsible for any of the company's legal obligations and debts
- partners can act on behalf of the others when entering and negotiating contracts with third parties
- partners have easy means of dissolving or general partnerships dissolve automatically in the case of death, resignation or bankruptcy

2. Limited partnership

Limited partnerships or LPs are legal business entities authorised by respective bodies, including HMRC. They consist of two parties – general partners with unlimited liability and special partners with limited liability in regards to their capital contribution. The general partners are fully responsible for the company, while the limited or silent partners provide money but don't actively manage the business. They may advise general partners and inspect the company's books:

Features of limited partnerships:

- usually have one or more general partners and one or more special-limited partners
- invest in the company for financial return but aren't responsible for liabilities and debts
- have total liability over the company's legal obligations and debts
- don't dissolve by death, lunacy or bankruptcy of a special partner
- can't assign their shares to an outsider without the consent of general partners
- can't withdraw any part of the capital they contribute
- more stable than general partnerships

3. Limited liability partnership (LLP)

Limited liability partnerships or LLPs are formal legal entities that operate as a general partnership. The partnership exists as its own legal individual and borrows money and owns assets on its own account. LLPs have two designated members: general partners with full management control over the company and limited partners with no personal liability beyond their investment in the business. The partnership is essentially a hybrid of a private limited company and an ordinary partnership structure, combining the benefits of both forms of business entities.

Features of LLPs:

- Individual partners aren't personally liable for any debts the business incurs.
- General partners distribute the company's profits as per the agreement and each member pays their own personal income tax.
- Individual partners aren't responsible for the wrongful acts, errors and omissions of their fellow partners.
- Limited partners don't participate in the daily operations and general management of the business.
- General partners accept full management control for partnership liabilities.

Partnership

Advantages

- Ease of Start-up
- Availability of Capital and Credit
- Personal Interest
- Combined Business Skills and Knowledge
- Retention of Profits
- No Special Taxes

Disadvantages

- Unlimited Liability
- Management Disagreements
- Lack of Continuity
- Frozen Investment

Corporation

A **corporation** is an organization—usually a group of people or a company—authorized by the state to act as a single entity (a legal entity recognized by private and public law as "born out of statute"; a legal person in a legal context) and recognized as such in law for certain purposes.

1. Closed Corporation
   - Stock is owned by relatively few people and is not sold to the general public.

2. Open Corporation
   - Stock can be bought and sold by any individual.

Corporation

Advantages	Disadvantages
• Ease of Start-up • Availability of Capital and Credit • Personal Interest • Combined Business Skills and Knowledge • Retention of Profits • No Special Taxes	• Unlimited Liability • Management Disagreements • Lack of Continuity • Frozen Investment

Questions

1. What is a sole proprietorship?
2. List two main advantages of a sole proprietorship.
3. What is the main disadvantage of a sole proprietorship regarding liability?
4. Why is a sole proprietorship considered the simplest form of business?
5. efine a partnership in economic activity.
6. Who can be partners in a partnership?
7. What are the three common types of partnerships?
8. In a general partnership, how are profits and ownership usually divided?
9. What happens to a general partnership if one partner dies or resigns?
10. What distinguishes a limited partnership from a general partnership?
11. Who are “silent partners” in a limited partnership?
12. Why are limited partnerships more stable than general partnerships?
13. What makes a limited liability partnership (LLP) different from other forms of partnerships?
14. Are individual partners in an LLP personally liable for company debts? Explain.
15. In an LLP, who has full management control over the partnership?
16. Define a corporation.
17. Why is a corporation considered a “legal person” in law?
18. What are two advantages of forming a corporation compared to partnerships?
19. What is the role of the state in the creation of a corporation?
20. Compare partnerships and corporations in terms of liability and legal personality.

Thanks for your attention !