Chapter 4: Types of Business Organization

Sole Traders

- A sole trader is a business owned by one person

Advantages

- Easy to set up business
- Makes all the decisions
- Has complete control
- Keeps the profit

Disadvantages

- Unlimited liability
- May not be able to raise sufficient funds for expansion
- May have to work long hours
- Difficult to compete with larger rival firms
- May not have skills to run a business

Liability

- Limited liability means that the liability of shareholders in a company is limited to the amount they invested
- Unlimited liability means that the owners of a business can be held responsible for the debts of the business they own. Their liability is not limited to the investment they made

Partnerships

- Partnership is a form of business in which two or more people agree to jointly own a business
- A partnership agreement is the written and legal agreement between business partners. It is not essential for partners to have such an agreement but it is recommended.

Advantages

- Easy to set up Deed of Partnership
- Partners invest in the business so have greater access to funds
- Shared decision making
- Shared management and work load

Disadvantages

- Unlimited liability

- Shared profits
- Business ceases to exist if one partner leaves
- Decision binding on all partners
- Difficult to raise funds

- An unincorporated business is one that does not have a separate legal identity. Sole traders and partnerships are unincorporated businesses

- Incorporated business are companies that have separate legal status from their owners

- Shareholders are the owners of a limited company. They buy shares which represent part ownership of a company

- Articles of Association- This contains the rules under which the company will be managed-the rights and duties of all the directors, rules concerning the election of directors and the holding of official meetings; and the procedure to be followed when issuing shares

- Memorandum of association- This contains very important information about the company and the directors. The official name and address of the registered offices of the company must be stated. The objectives of the company must be states as well as the number of shares to be bought by each of the directors

Private and Public Limited Companies

	Private Limited Companies	**Public Limited Companies**
Owners	Usually very a small number of shareholders.	Usually a very large number of shareholders
Size	Usually fairly small	Most common form of very large companies
Sales of shares by the company	Can only be sold privately, often to family members, friends or employees	Can be offered for sale to the general public and other organizations
Sales of shares by the shareholder	Often difficult to sell as must be sold privately and with the agreement of other shareholders	Quick and easy to sell as they can be offered for sale to the public

Control	Ownership is not separated control	The Board of Directors is appointed by shareholders at the Annual General Meeting who control major decisions. Ownership and control are separated
Raising additional capital through share issue	May be difficult to raise additional capital as shares cannot be sold to the general public	If successful then can often raise very large sums quite easily through the sale of additional shares
Borrowing Finance	Difficult to borrow finance due to size and lack of collateral	Can often raise very large sums at good rates of interest because of their reputation and valuable collateral.

Private limited companies

Advantages

- Raise capital from sale of shares
- Limited liability for shareholders
- Separate legal identity
- Continuity

Disadvantages

- Cannot sell shares to public
- Legal formalities
- Accounts must be made available for public to see
- Not easy to transfer shares

Public limited companies

Advantages

- Limited liability
- Can sell shares to public
- Rapid expansion possible (specialist managers appointed)
- Continuity

Disadvantages

- Legal formalities
- Disclosure of accounts and other information

- Divorce between ownership and control
- Expensive to go public

- An annual general meeting is a legal requirement for all companies. Shareholders may vote on who they want to be on the Board of Directors for the coming year

- Dividends are payments made to shareholders from the profits (after tax) of a company. They are the return to the shareholders for investing in the company

Joint Ventures

- A joint venture is when two or more businesses agree to start a new project together, sharing capital, the risk and profits

Advantages

- Sharing of costs
- Local knowledge
- Risks are shared

Disadvantages

- Profits have to be shared
- Disagreements over important decisions that might occur
- Clash of leadership styles

Franchising

- A franchise is a business based upon the use of brand names, promotional logos and trading methods of an already successful business. The franchisee buys the license to operate this business from the franchisor.

Advantages to the Franchisor

- Expansion is faster
- Management is the responsibility of the franchisee
- All products sold must be obtained from the franchisee

Disadvantages to the Franchisor

- Bad reputation due to poor management
- Franchisee keeps profit

Advantages to the Franchisee

- Chances of failure are reduced
- Franchisor pays for advertising
- All supplies obtained from a central source
- Less decision making
- Training for staff

Disadvantages to the Franchisee

- Less independence
- May be unable to make decisions that would suit local area
- License fee must be paid to the franchisor and a percentage of the possible turnover

- The franchisee contributes: capital, enterprise and management

- The franchisor contributes: original idea, use of brand name and products, and advertising and training

Public Corporations

- These are wholly owned by the state or central government. They are usually businesses which have been nationalized. This means that they were once owned by private individuals, but were purchased by the government. Public corporations are owned by the government but it does not directly operate the business.