# Lecture 9 Answers

# Question One

Advantages of setting up the partnership

Nick may well be correct in suggesting that there are some commercial advantages in entering into a partnership. A larger business may indeed be able to obtain better discounts on bulk purchases. This could mean that the partnership could be more profitable than the individual sole trader businesses. It could also be in a better position to compete on price if there are price-cutting competitors. There could be advantages if Nick and Paul have complementary skills.

Disadvantages of setting up the partnership

However, the proposal is really quite risky. Partners are responsible in law for the consequences of each other’s actions. This can lead to unexpected problems even in situations where the partners know each other well. In this particular situation, Paul and Nick do not appear to know each other at all well. The fact that Nick wants to dispense with what he refers to as ‘red tape’ does not bode well. Although there is no legal requirement to have a written partnership agreement it would be of particular importance where the partners are not well acquainted with each other. As well as the particular disadvantages of this proposed partnership there are more general disadvantages applicable to all partnerships. Partners bear unlimited liability and where business debts cannot be paid, the partners’ own personal property may have to be sold to raise funds.

Formalities involved in setting up a partnership

As noted above, there is no strict legal necessity for a partnership agreement, although it is usually advisable to have one drawn up and agreed. Starting up a company does involve form-filling, as Nick says, but it is a relatively straightforward procedure. Partners are taxed as individuals on their share of partnership profits, and, apart from the additional complexities involved in calculating shares of the profits, there is little difference between partners and sole traders in this respect. As in the case of sole traders, partnerships do not have to publish any financial information.

# Question Two

The purchase of the workshop will benefit the business in the longer-term and so long-term finance is likely to be the most appropriate. A combination of the following sources of finance might be suitable:

• Existing business resources – if the business has a cash surplus that it does not currently need, this could be invested in the workshop.

• Juan’s own funds – he may be able to introduce additional capital into the business from his own savings.

• Long-term borrowing – a mortgage loan taken out over a reasonably long period (of, say, ten years) may be suitable. Juan will need to investigate the costs of borrowing and should plan carefully to ensure that the business can cover the outlay in loan repayment and interest.