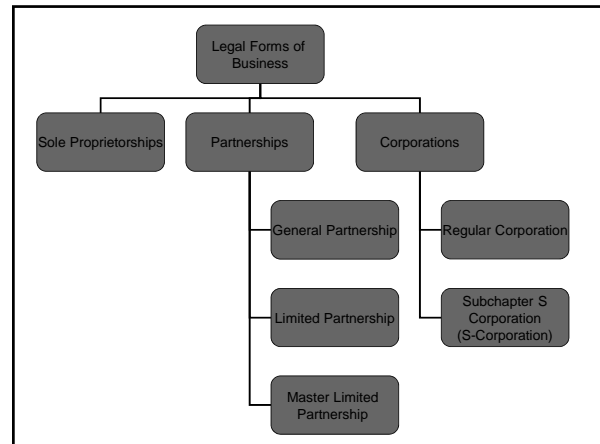


Forms of Business Organization

Chapters 18 & 19



Sole Proprietorships

- Business owned (and usually operated) by one person
- Simplest form of business ownership
- Most popular form of business organization – 72.2% of all
- Most common in:
 - Retailing
 - Service
 - Agriculture

Sole Proprietorship -- Advantages

- Ease of Startup
 - Little legal documentation
 - No co-owners to consult
- Least expensive to start
- Pride of Ownership
- Retention of profits
- Flexibility
- No Business Income Tax

Sole Proprietorship -- Disadvantages

- Unlimited Liability
- Limited Life – Business ends when owner leaves the business
- Limited Access to Start-up Capital
- Limited Access to Credit
- Limited Management Expertise
- Difficulty in Hiring Employees
- Proprietor not considered an employee

Partnerships

- Two or more owners
- Least numerous form – 7.7% of all businesses
- Partnership Agreement
 - Specifies rights and obligations of partners
 - If written, called the Articles of Partnership (Articles of Co-partnership)

Partnership -- Advantages

- Greater Access to Capital
- Greater Access to Credit
- Retention of Profits
- More Management Expertise
- No Business Income Tax

Partnership -- Disadvantages

- Shared Profits
- Unlimited Liability for "General Partners"
- Each partner has "Agency" power
- Limited Life
 - Business ends when any partner withdraws
- Management Disagreements
- Frozen Investment

Types of Partners

- General Partner
 - Unlimited Liability
 - Assumes Management Role
- Limited Partner
 - Liability limited to Investment
 - May not take active managerial role
- Every partnership must have at least one general partner

Types of Partners

- General Partnership
 - All partners are general partners
- Limited Partnership
 - One or more limited partners
- Master Limited Partnership
 - Owned & managed like a corporation
 - Taxed like a partnership
 - Shares may be sold

Corporations

- Generally larger than other forms (Except for S-Corporation)
 - 20.1% of all U.S. Businesses
 - Account for 87.1% of all U.S. Business Income
- Considered a separate legal entity
 - Owners called "Stockholders" or Shareholders"
- Ownership evidenced by "Stock Certificate"
- Governed by "Board of Directors"

Corporations -- Advantages

- Limited Liability
- Ease of Ownership Transfer
- Unlimited Life
- Greater Access to Capital
- Specialized Management Expertise

Corporations -- Disadvantages

- More difficult & costly to form
 - Requires a “Corporate Charter”
- Subject to greater governmental scrutiny
- Diluted earnings
- Double taxation

Corporations vs. Sole Proprietorships

	<u>SP</u>	<u>Corp</u>
Income	\$1,000,000	\$1,000,000
Expenses	<u>500,000</u>	<u>500,000</u>
EBT	\$500,000	\$500,000
(Assume Business Tax Rate = 50%)		
Business Tax	<u>0</u>	<u>250,000</u>
Net Profit	\$500,000	\$250,000
(Assume a 30% Personal Tax Rate)		
Personal Tax	<u>150,000</u>	<u>75,000</u>
\$ to Owners	\$350,000	\$175,000

Corporate Charter

- Legal Permission to Operate as a Corporation
 - Requires a “Corporate Charter”
- Issued by state
- May not conduct business as a corporation without a charter

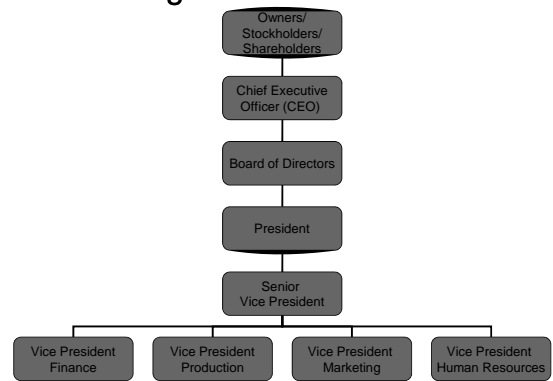
Contents of a Corporate Charter

- Company Name & Address
- Names & addresses of Incorporators
- Purpose of the Corporation
- Maximum amount of stock & Classes of Stock to be issued
- Rights & Privileges of stockholders
- Length of time the corporation is to exist

Stockholder Rights

- Common Stock
 - Votes in corporate matters
 - One vote per share owned
- Preferred Stock
 - No voting rights
 - Dividend claims are paid 1st
- Dividend
 - Distribution of earnings to the stockholders of a corporation

Organizational Chart



Types of Corporations

- **Government-Owned Corporation**
 - aka “Public Corporation”
 - Owned & operated by government
 - Post office, NASA, FDIC
- **Quasi-Government Corporation**
 - Aka “Quasi-Public Corporation”
 - Privately owned, government controlled monopoly
 - Public utilities, Fannie Mae, Freddie Mac, Sallie Mae
- **Private Corporation**
 - Owned by individuals or other companies

Types of Corporations

- **Not-For-Profit Corporation**
 - Organized to provide a social, educational, religious, or other service
 - Habitat for Humanity, Red Cross
- **For-Profit Corporation**
- **Closed Corporation**
 - Stock owned by relatively few people
 - Stock not sold to general public
- **Open Corporation**
 - Stock is bought and sold on security exchanges
 - Can be purchased by any individual

Types of Corporations

- **S-Corporation (Subchapter-S Corporation)**
 - Corporate structure designed for small business
 - Taxed as a partnership if there are 75 or fewer stockholders
 - No non-resident alien stockholders
 - Only one class of stock
- **Limited-Liability Company (LLC)**
 - Combines the benefits of a corporation & partnership
 - Not limited to 75 stockholders

Mergers & Acquisitions

- **Hostile takeover**
- **Types of mergers**
 - Horizontal: Similar products / services
 - Vertical: Different but related firms
 - Conglomerate: Completely different industries
- **Merger Trends**
 - Divestiture
 - Leveraged Buyout (LBO)

Franchising

- **Franchise**
 - License to operate an individually owned business as though it were part of a chain of outlets or stores
 - The business itself
- **Franchising**
 - Actual granting of a franchise

Franchising

- **Franchisor**
 - Supplies a known & advertised business name
 - Supplies management skills
 - Supplies training & materials
 - Supplies method of doing business
- **Franchisee:**
 - Supplies labor & capital
 - Operates the franchised business
 - Agrees to abide by the franchise agreement

Franchising Advantages

- Franchisor
 - Fast, Selective Distribution
 - Motivated Franchisee
- Franchisee
 - Opportunity to start a business
 - Business Experience of others
 - Nationally recognized name
 - National promotional campaigns

Franchising Disadvantages

- Mainly from Franchisee's Viewpoint:
 - Franchisor's contract can dictate every aspect of the business
 - Pay for security
 - Long hours
 - Competition from same company