

Forms of Business Organisation

The form of business organisation determines its external existence and the other parties recognise it through this existence.

Meaning: The forms of business organisation are related with ownership and ownership is a legal concept which determine the authority and responsibility of the owners. The authority and responsibility of the owners keep on changing along with changing forms of ownership.

Forms of Business Organisation

Many types of business organisations on the basis of ownership. Some business are managed by single individual, some business are managed by many people collectively in the form of partnership firm, while some other business are run in the form of a joint stock company.

- ⇒ Sole proprietorship
- ⇒ Partnership
- ⇒ Cooperative
- ⇒ Joint-Stock Company.

Sole Proprietorship

Sole proprietorship is a form of business organisation in which an individual brings his own capital, manages the business himself and is solely responsible for the results of its operations also known as sole trader. In sole proprietary business only one person is the owner, manager, controller, risk bearer i.e. all in one.

Origin of Sole Proprietorship

Sole tradership is an ancient and simple form of organisation. Historically, this form of organisation took birth in the same shape, it is said that this organisation was evolved at the time when the man started living in family. As the time changed its shape and size went on changing. This organisation is also known as sole proprietorship, individual proprietorship and single entrepreneurship.

Definitions of Sole Proprietorship

Kimball and Kimball: “The individual proprietor is the supreme judge of all matters pertaining to his business subject only to the general laws of the land and to such special legislation as may affect its particular business.”

James Stephenson : “A sole trader is a person who carries on business exclusively by and himself. He is not only the owner of the capital of the undertaking, but is usually the organiser and manager and takes all the profits or responsibility for losses.”

Peterson and Plowman: “A sole proprietorship is a business unit whose ownership and management are vested in one person. This individual assumes all risk of loss or failure of the enterprise and receives all profits from its successful operation.”

Characteristics or Features of Sole Proprietorship

SMALL BUSINESS



Characteristics of Sole Proprietorship

1. **Sole ownership:** The proprietorship business is solely owned by an individual. He contributes the entire capital. However, he may borrow the funds from his relations, friends, banks or financial institutions.
2. **Owner-cum-manager:** The sole proprietor is both an owner as well as manager. He can exercise full control over the business. He can take decisions quickly.
3. **Entire risk:** As a sole owner, he bears the entire risk. He enjoys all the profits and suffers all the losses.
4. **Unlimited liabilities:** The liabilities of the sole proprietor are unlimited. Personal property of the sole proprietor can be used to pay his business liability.
5. **No separate entity:** A proprietorship business has no separate existence from its ownership. There is no distinction between the business and the owner. Any profit or loss of the business is the profit or loss to the sole proprietor.

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6. **Freedom from government control:** There is complete freedom from government control. No permission is required from local authorities. Formation and operation of a sole proprietary business is very easy.
 7. **Common identity:** A sole tradership concern has no separate legal entity independent of the owner. The owner owns everything the business owns and he owes everything the business owes. Thus, there is no differences between the sole trader and his business.
 8. **Capital:** In sole tradership, the capital is employed by the owner himself from his personal resources. He may also borrow money from his friends and relatives for investment in the business.

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9. **Management and control:** Sole tradership is one man show. The sole trader provides management to the business. He takes all the decisions, procures materials and other resources, employs workers and directs and controls the affairs of the enterprise. He is not required to consult anyone else in taking any decision. The sole trader may delegate some of his authority to his employees, but the ultimate authority to manage and control rests with him.
 10. **No sharing of profits and losses:** The surplus arising in the business of the sole trader entirely belongs to him. Similarly all the business losses and risks are to be borne by the sole trader alone.

Legal position of a sole proprietor

1. In the eyes of law business and businessman have separate entity,
2. There is no legal restriction in the establishment of a business,
3. A sole trader has unlimited liability,
4. A sole trader has no separate law or act.

Advantages of sole proprietorship

1. **Ease of formation:** No legal formalities are required to form and operate the sole proprietorship. However, the sole trader may be required to obtain permission of the local authorities in certain cases to run a particular business or to get the firm registered with appropriate authorities.
2. **Direct incentive:** In a sole proprietary business there is direct relationship between efforts and reward which serves as a powerful incentive to the sole proprietor to put in his best efforts. He knows that he is to bear all the losses and he will get all the profits if he works hard.
3. **Quick decision making:** The sole proprietorship can take business decisions quickly. He can take full advantages of business opportunities as and when they arise.
4. **Personal relations:** The sole trader is able to maintain personal relations with his customers. He is able to know his customers personally. He can cater to their individual tastes and needs. As such his customers feel satisfied. This results into increased sale.

5. **Secrecy:** The sole proprietor need not share the secrets of his business. He has full control over his business.
6. **Freedom of initiative:** Since sole proprietor is in full control of his enterprise, he can take full initiative to introduce any innovation or change.
7. **Creation of employment opportunities:** Sole proprietary business uses labour intensive techniques of production, thereby creating larger employment opportunities.
8. **Checks concentration of economic power:** Sole proprietorship helps in checking concentration of economic power.
9. **Easy coordination:** A sole proprietor can coordinate the various activities of his enterprise easily as he can take decisions himself. He need no consult any one else.
10. **Economy:** Sole proprietor can eliminate wasteful expenditure. He knows that it is his own money which should be spent wisely.

Demerits of Sole proprietorship

1. **Limited resources:** The financial resources of a sole proprietor are limited. He cannot take the risk of borrowing and investing large sums of money in his business. Therefore, sole proprietary business cannot be carried on at a large scale.
2. **Unlimited liabilities:** One of the most serious limitations of a sole proprietor is his unlimited liabilities. The sole proprietor will be reluctant to introduce new technology and take up risky adventures.
3. **Limited Managerial skill:** Sole trader has limited organising power and managerial skill. No individual can be expert in all areas.

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4. **Small size:** A sole proprietary business is small in size. As such it is not suitable for large scale business. The benefits of specialisation and economies of large scale are not available to such business. It cannot grow in size due to limited finance and managerial ability.
 5. **Instability:** The sole proprietary business may come to an end with the death, illness or insolvency of the proprietor.
 6. **Too much dependence on the owner:** In sole proprietary business there is too much dependence on the sole proprietor. In his absence the business may suffer loss due to negligence of assistants, loss of personal contact with customers, loss of customers to competitors etc.
 7. **Hasty decisions:** A sole trader may make hasty decisions. There is no one to help him in making decisions.

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8. **Risk of incompetent inheritance:** On the death of the sole proprietor the business may suffer heavy losses and may be closed down if it passes into incompetent hands.
 9. **Unsuitable for developing business:** Last but not the least sole proprietorship form is unsuitable for a business which is gradually expanding in size.

Hence, sole proprietary business organisations is suitable for the following kinds of business:

- (i) Where little or no capital is needed
- (ii) Where there is no risk
- (iii) Where quick decisions are necessary
- (iv) Where the customers require personal attention
- (v) When special attention is required to meet the tests of the customers.

Partnership

Indian Partnership Act, Sec-4, “Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.”

A partnership is formed by two or more members, each of whom is liable for the firm's debts. Two or more individual may form a partnership by making a written or oral agreement stating that they will carry on a business jointly and will share the profits therefrom. A partnership is, therefore, a group of persons who have contributed the capital for setting up some business.

Partnership-Introduction

A partnership is a voluntary association of two or more persons who agree to carry on some business jointly and share its profits and losses. The persons who enter into partnership are individually called 'partners' and collectively a 'firm'. The name under which they carry on business is called the 'firm name.'

Prof. Mac Naughton, "Partnership results from the desires of business to take advantages of complementary ability and to raise more capital."

BUSINESS STRUCTURES:
Partnerships



Characteristics of Partnership

1. **Agreement between two or more persons:** Partnership is an agreement between two or more persons. The minimum number of partners is two and the maximum number of person according to Rule 10 of the 2014 provides the maximum limit as 50 partners.
2. **Legal business:** The business carried on by the partnership firm must be legal. It means that stealing, burglary, pick-pocketing, smuggling etc. are not the business in the eyes of law.
3. **Contractual relationship:** Partnership originates from the mutual contract among partners. This contact is made through their mutual relationship. Any person who cannot enter into contract, cannot become partner of a firm e.g. minors, lunatics etc. cannot become partners.

Characteristics of Partnership

4. **Profit motive:** The business carried on by the partnership firm must have profit motive. In this way, orphanage, free dispensary, charitable trusts etc. can not become partnership.
5. **Principal-Agent relationship:** Principal-agent relationship means that just as an owner is responsible for any contract entered into by his agent/s operating within the limits of his/their authority, similarly, a partner can bind all the partners with his activities. In this way every partner plays a double role of an owner and an agent.

Characteristics of Partnership

- 6. Unlimited liability:** Every partner of the firm is individual and jointly liable for the dues and debts of the firm. In other words, the liability of individual partner is not restricted to the amount of capital invested by him. It may be even more than the, if other partners are financially unsound/insolvent.
- 7. No separate entity:** Partnership and partners are one in the eyes of law. All the partners are liable jointly as well as severally for the contracts made by the firm.

Characteristics of Partnership

8. **Utmost good faith:** Partners are individually different it will be fatal for the business if they behave individually in their own way in the business affair. Partners must integrates their efforts and work as team with utmost good faith on each other.
9. **Restriction on transfer of interest:** The partners can not transfer their interest i.e., share in the business to other persons. Any change in the partnership can be effected through mutual consent. A new partner can be admitted or old partners may retire with the mutual consent.
10. **Definite name of the firm:** The name which the partners use for conducting business, is called name of partnership. A partnership must have a definite name.

Characteristics of Partnership

11. **Mutual agency:** Every partner is the agent of the firm. Partners are also the mutual agent of each other.
12. **Non-transferability of share:** No partner can transfer his/her share in the partnership to any other person. He can do so only with the consent of other partners. If the partner wants to leave the firm then he can do so by giving a notice of retirement.
13. **Registration of partnership:** According to Partnership Act, 1932, it is not compulsory for a partnership firm to get itself registered. However, the partners prefer to get the partnership firm registered because there are certain advantages of registration.
14. **Only individual as a partner:** An important characteristics of partnership is that only an individual can be a partner not any firm or institution.

Sole Proprietorship



Partnership



Advantages of Partnership

1. **Easy to start:** There is no complicated legal procedure to start partnership. It does not take much expenditure to start partnership. It can be started very easily.
2. **Sufficient capital:** Partnership has more capital resources as compared to sole trade. It can even get larger amount of loans from other institutions on easy terms.
3. **Specialization in management:** A division of work in partnership is done in accordance with scientific management principles. Work is given to partners as per their capabilities and they get specialisation in their work.
4. **Balanced decision:** Decision are taken jointly, by consulting each other, therefore, the partnership is able to take balanced decision.
5. **Democratic organisation:** All the partners have a right to take part in the working of partnership. All the partners are consulted while taking any decision. Therefore, partnership has a democratic system.

Advantages of Partnership

6. **Secrecy:** Partnership does not have to get its accounts published like joint stock company. Its partners know about its affairs. Therefore, partnership is able to maintain secrecy in its functioning.
7. **Advantage of unlimited liability:** Since liability of partners is unlimited, therefore, they take most care in discharging their duties.
8. **Protection of minority interest:** In partnership, minority partners have legal protection. In taking every decision, each and every partner is consulted.
9. **Combined resources:** In partnership, partner's capital, energy, knowledge, experience etc. act jointly and more effectively.

Advantages of Partnership

- 10. Flexibility:** Partnership has greater flexibility. The expansion of business, objects, capital and number of partner can be changed according to situation without any legal obstacle. Running business can be replaced by some other business very easily.
- 11. Protection of minor:** A minor cannot become a partner of a firm. But with the consent of all partners, a minor can be admitted to profits of the business. A minor partner has limited liability.
- 12. Registration not compulsory:** It is not necessary for the partnership to get it registered. The partners may or may not get the partnership registered.

Advantages of Partnership

- 13. More suitable to risky business:** Partners have greater capacity to bear risk as the risk gets divided among partners. According to the saying 'more risk, more profit' greater profit can be earned in partnership by taking more risk.
- 14. Personal relations and good faith:** Due to limited numbers of partners, they develop direct relations with customers and employees. It improve mutual co-operation.

Disadvantage of Partnership

1. **Difficulty in transfer of interest:** No partner can transfer his interest in partnership without the consent of all the partners. Due to this limitation, lots of people hesitate to invest money in partnership.
2. **Delay in decision:** Decision making in partnership requires consent of all partners. It results in delay in decision making.
3. **Unlimited liability:** Liability of partnership is unlimited. Even the personal assets of partners can be used to meet firm's debts.
4. **Instability:** Partnership has an uncertain future. Death of a partner, insanity, insolvency etc. ends the partnership. Apart from that any partner can end partnership by giving a notice to all partners.
5. **Responsibility after winding up:** Normally, the liabilities of a business end with the closer of business. But according to Partnership Act, responsibility of partners does not end until they are given public notice of winding up of partnership.

Disadvantage of Partnership

6. **Conflicts and frictions:** Partnership lacks centralized management. As every partner has a right to manage partnership, but leads to conflict and frictions. All this becomes harmful for the future of partnership.
7. **Limited resources of capital:** Partnership has larger resources as compared to Sole-Trade but with the expansion of business, these sources become insufficient. This is because of limited membership.
8. **More expenses:** Since the burden of expenditure is borne by all not by an individual, therefore, partners spend lavishly, as they feel that they, as individuals, are not alone to bear the losses.
9. **Risk of implied authority:** Every partner is representative of the firm. He binds the firm for acts done by him. Any dishonest or inefficient partner may result losses to other partners through his misdeeds.
10. **Affects of mutual differences:** Every partner knows about the secrets and records of partnership. In the event of mutual conflicts he may pass on these secrets to the competitors of business. This may result loss to the firm.

Kinds of Partnership

1. **Partnership at will:** When a partnership is made for an indefinite period, with a view to established a business, it is called partnership at will. This type of partnership can be ended any time, by giving a necessary notice by one or all the partners.
2. **Particular partnership:** When a partnership is established to perform some specific object and it is ended when that object is accomplished, this partnership is called particular partnership.
3. **Fixed term partnership:** When partnership is established for a fixed period and it automatically comes to an end when this period expires, such partnership is called fixed term partnership.
4. **Continuing partnership:** In this kind of partnership no specific time to object is determined. This type of partnership goes on until it is ended by legal procedure.

Kind of partnership

5. **Legal partnership:** When all the rules and regulations of Partnership Act, 1932 and other related acts are followed in making and running partnership, it is called legal partnership.
6. **Illegal partnership:** When the proper laws are not followed in partnership e.g. number of partners is less than two or more than twenty, illegal objectives, admitting alien enemy as member of firm, etc, their such partnership is called illegal partnership.
7. **General partnership:** Such partnership, which has all the characteristics of a partnership.
8. **Limited partnership:** In general partnership, liabilities of all partners are unlimited. But in limited partnership, the liability of at least one partner should be limited. Such type of partnership is not in practice in India. This type of partnership exists in countries like England, America etc.