

CHAPTER 2

FORMS OF BUSINESS

ORGANISATION

FORMS OF BUSINESS ORGANISATION

If one is planning to start a business or is interested in expanding an existing one, an important decision relates to the choice of the form of organisation. The most appropriate form is determined by weighing the advantages and disadvantages of each type of organisation against one's own requirements..

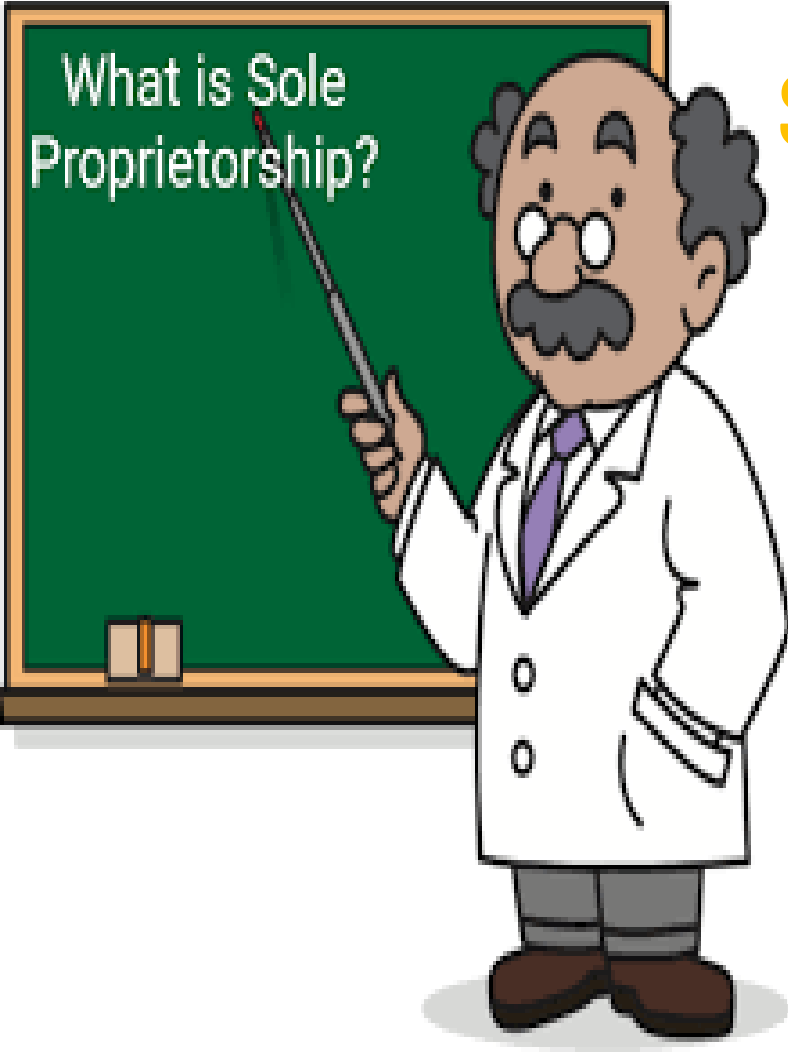
Various forms of business organisations include:

- Sole proprietorship,
- Joint Hindu family business,
- Partnership,
- Cooperative societies, and
- Joint stock company.



SOLE PROPRIETORSHIP





What is Sole
Proprietorship?

Sole proprietorship

Sole proprietorship refers to a form of business organisation which is owned, managed and controlled by an individual who is the recipient of all profits and bearer of all risks. This is evident from the term itself. The word “sole” implies “only”, and “proprietor” refers to “owner”. Hence, a sole proprietor is the one who is the *only owner* of a business.



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Sole trader is a type of business unit where a person is solely responsible for providing the capital, for bearing the risk of the enterprise and for the management of business.

J.L. Hansen

Sole Proprietorship is that form of business which has a single owner, who has the total responsibility of the business, who runs the business and also bears the risk on the failure of business.

Prof Hynes



Features

- Formation and closure
- Liability
- Sole risk bearer and profit recipient
- Control
- No separate entity
- Lack of business continuity



Merits

- Quick decision making
- Confidentiality of information
- Direct incentive
- Sense of accomplishment
- Ease of formation and closure



SOLE PROPRIETORSHIP

Limitations

- Limited resources
- Limited life of a business concern
- Unlimited liability
- Limited managerial ability





JOINT HINDU FAMILY BUSINESS



Joint Hindu family business

Hindu Undivided Family

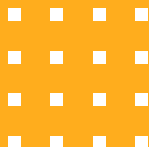


Joint Hindu family business is the oldest form of business organisation found only in India & governed by the Hindu Law. the business is owned and carried on by the members of the Hindu Undivided Family (HUF). The basis of membership in the business is birth in a particular family and three successive generations can be members in the business.



The business is controlled by the eldest member and is called *karta*.

All members have equal ownership right over the property of an ancestor and they are known as *co-parceners*.



Features

- Easy Formation
- Limited Liability
- Control
- Continuity
- Minor Members



Merits

- Effective control
- Continued business existence
- Limited liability of members
- Increased loyalty and cooperation



Limitations

- Limited resources
- Unlimited liability of *karta*
- Dominance of *karta*
- Limited managerial skills





PARTNERSHIP



PARTNERSHIP

Partnership serves as an answer to the needs of greater capital investment, varied skills and sharing of risks & management

The Indian Partnership Act, 1932 defines partnership as “the relation between persons who have agreed to share the profit of the business carried on by all or any one of them acting for all.”





Partnership is the relation between persons competent to make contracts who have agreed to carry on a lawful business in common with a view to private gain.

L H Haney

Partnership is the relation which subsists between persons who have agreed to combine their property, labour or skill in some business and to share the profits therefrom between them.

The Indian Contract Act 1872

Features

- Formation
- Liability
- Risk bearing
- Decision making and control
- Continuity
- minimum partners is two. maximum partners can be 100 or 50.
- Mutual agency



Merits

- Ease of formation and closure
- Balanced decision making
- More funds
- Sharing of risks
- Secrecy

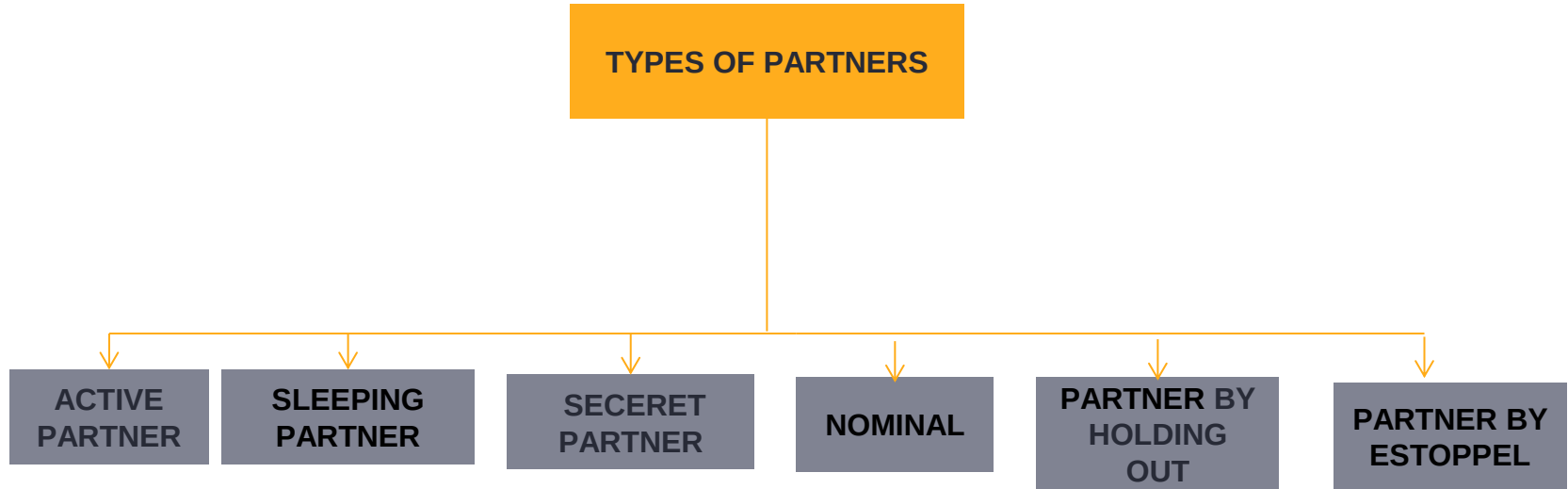


Limitations

- Unlimited liability:
- Limited resources:
- Possibility of conflicts:
- Lack of continuity:
- Lack of public confidence:



TYPES OF PARTNERS



TYPES OF PARTNERS

(i) Active partner: An active partner is one who contributes capital, participates in the management of the firm, shares its profits and losses, and is liable to an unlimited extent to the creditors of the firm. These partners take actual part in carrying out business of the firm on behalf of other partners.

(ii) Sleeping or dormant partner: Partners who do not take part in the day to day activities of the business are called sleeping partners. A sleeping partner, however, contributes capital to the firm, shares its profits and losses, and has unlimited liability.



(iii) Secret partner: A secret partner is one whose association with the firm is unknown to the general public. He contributes to the capital of the firm, takes part in the management, shares its profits and losses, and has unlimited liability towards the creditors.



(iv) Nominal partner: A nominal partner is one who allows the use of his/her name by a firm, but does not contribute to its capital. He/she does not take active part in managing the firm, does not share its profit or losses but is liable, like other partners, to the third parties, for the repayments of the firm's debts

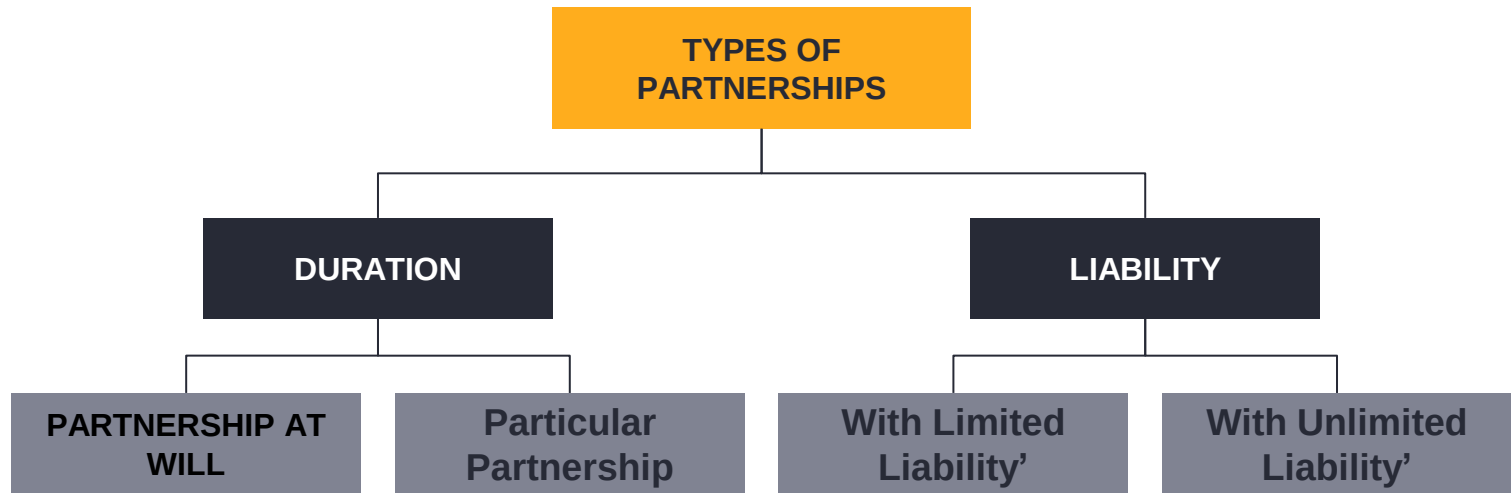


TYPES OF PARTNERS

(v) Partner by estoppel: A person if, through his own initiative, conduct or behaviour, he gives an impression to others that he is a partner of the firm. He is liable for the debts of the firm because in the eyes of the third party he is considered partner, even though he did not contribute capital or take part in its management.

(vi) Partner by holding out: a person who though is not a partner in a firm but knowingly allows himself to be represented as a partner in a firm. he will be liable for debts extended to firm due to such representation. to save himself from such a liability, he should immediately issue a denial, clarifying he is not a partner in the firm.

TYPES OF PARTNERSHIPS



Classification on the basis of duration

(i) Partnership at will: This type of partnership exists at the will of the partners. It can continue as long as the partners want and is terminated when any partner gives a notice of withdrawal from partnership to the firm.

(ii) Particular partnership: Partnership formed for the accomplishment of a particular project say construction of a building or an activity to be carried on for a specified time period is called particular partnership. It dissolves automatically when the purpose for which it was formed is fulfilled or when the time duration expires.

Classification on the basis of liability

(i) General Partnership: In this the liability of partners is unlimited and joint. The partners enjoy the right to participate in the management of the firm and their acts are binding on each other as well as on the firm. Registration of the firm is optional.

(ii) Limited Partnership: In limited partnership, the liability of at least one partner is unlimited whereas the rest may have limited liability. Such a partnership does not get terminated with the death, lunacy or insolvency of the limited partners. The limited partners do not enjoy the right of management and their acts do not bind the firm or the other partners. Registration of such partnership is compulsory. The idea is to enable the partnership firms to attract equity capital from friends and relatives

Minor as a Partner

a minor can be admitted to the benefits of a partnership firm with the mutual consent of all other partners. His liability is limited to the extent of his capital. He will not be eligible to take an active part in the management of the firm. Thus, a minor can share only the profits and can not be asked to bear the losses. he can inspect the accounts of the firm.

on attaining majority, the minor has to decide whether he would like to become a partner in the firm. He has to give a public notice of his decision within six months of attaining majority else he will be treated as a full-fledged partner



Partnership Deed

a clear agreement oral or written with respect to the terms, conditions and all aspects is essential so that there is no misunderstanding among the partners. Even though it is not essential, it is advisable to have a written. The written agreement which specifies the terms and conditions that govern the partnership is called the partnership deed.



The partnership deed generally includes :

- Name of firm
- Nature of business and location of business
- Duration of business
- Investment made by each partner
- Distribution of profits and losses
- Duties and obligations of the partners
- Salaries and withdrawals of the partners
- Terms governing admission, retirement and expulsion of a partner
- Interest on capital and interest on drawings
- Procedure for dissolution of the firm
- Preparation of accounts and their auditing
- Method of solving disputes

Registration

Registration of a partnership firm means the entering of the firm's name, along with the relevant prescribed particulars, in the Register of firms kept with the Registrar of Firms of the state. It provides conclusive proof of the existence of a partnership firm.

It is optional, but The consequences of non-registration of a firm According to the India Partnership Act 1932 are as follows:

- (a) A partner of an unregistered firm cannot file a suit against the firm or other partners,
- (b) The firm cannot file a suit against third parties, and
- (c) The firm cannot file a case against the partners.



Procedure for getting a firm registered

1. Submission of application in the prescribed form to the Registrar of firms. The application should contain the following particulars:

- Name of the firm • Location of the firm
- Names of other places where the firm carries on business
- The date when each partner joined the firm
- Names and addresses of the partners • Duration of partnership

This application should be signed by all the partners.

2. Deposit of required fees with the Registrar of Firms.

3. The Registrar after approval will make an entry in the register of firms and will subsequently issue a certificate of registration.



COOPERATIVE SOCIETY



COOPERATIVE SOCIETY



The cooperative society is a voluntary association of persons, who join together with the motive of welfare of the members. They are driven by the need to protect their economic interests in the face of possible exploitation. The cooperative society is compulsorily required to be registered under the Cooperative Societies Act 1912. with the consent of at least ten adult persons The capital of a society is raised from its members through issue of shares. The society acquires a distinct legal identity after its registration.



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Cooperative is a form of organisation wherein persons voluntarily associate together as human beings on the basis of equality for the promotion of an economic interest for themselves.

E. H. Calvert

Cooperative organisation is “a society which has its objectives for the promotion of economic interests of its members in accordance with cooperative principles.

The Indian Cooperative Societies Act 1912



Features

- Voluntary membership:
- Legal status:
- Limited liability:
- Control:
- Service motive



Merits

- Equality in voting status:
- Limited liability:
- Stable existence:
- Economy in operations
- Support from government:
- Ease of formation



Limitations

- Limited resources:
- Inefficiency in management:
- Lack of secrecy:
- Government control:
- Differences of opinion



- (i) **Consumer's cooperative societies:** The members comprise of consumers desirous of obtaining good quality products at reasonable prices. It purchases goods in bulk directly from the wholesalers and sells goods to the members, thereby eliminating the middlemen. Profits, if any, are distributed to members.
- (ii) **Producer's cooperative societies:** The society aims to fight against the big capitalists and enhance the bargaining power of the small producers. It supplies raw materials, equipment and other inputs to the members and also buys their output for sale. Profits are generally distributed on the basis of their contributions to the total production
- (iii) **Marketing cooperative societies:** The society aims to eliminate middlemen and improve competitive position of its members by securing a favourable market for the products. It pools the output of members and performs marketing functions to sell the output at the best possible price. Profits are distributed as per member's contribution to pool of output.
- (iv) **Farmer's cooperative societies:** The aim is to gain the benefits of large scale farming and increase the productivity. Such societies provide better quality seeds, fertilisers, machinery and other modern techniques for use in the cultivation of crops. This helps in improving the yield and returns to the farmers,
- (v) **Credit cooperative societies:** The members comprise of persons who seek financial help in the form of loans. The aim of such societies is to protect the members from the exploitation of lenders who charge high rates of interest on loans. Such societies provide loans to members out of the amounts collected as capital and deposits and charge low rates of interest.
- (vi) **Cooperative housing societies:**
The members of these societies consist of people who are desirous of procuring residential accommodation at lower costs. These societies construct flats or provide plots to members



COMPANY



COMPANY

A company can be described as an artificial person having a separate legal entity, perpetual succession and a common seal. The company form of organisation is governed by The Companies Act, 2013. As per section 2(20) of Act 2013, The shareholders are the owners of the company while the Board of Directors is the chief managing body elected by the shareholders. The capital of the company is divided into smaller parts called 'shares' which can be transferred freely from one shareholder to another person (except in a private company).

Features

- Artificial person
- Separate legal entity:.
- Formation:
- Perpetual succession:
- Control:
- Liability:
- Common seal
- Risk bearing



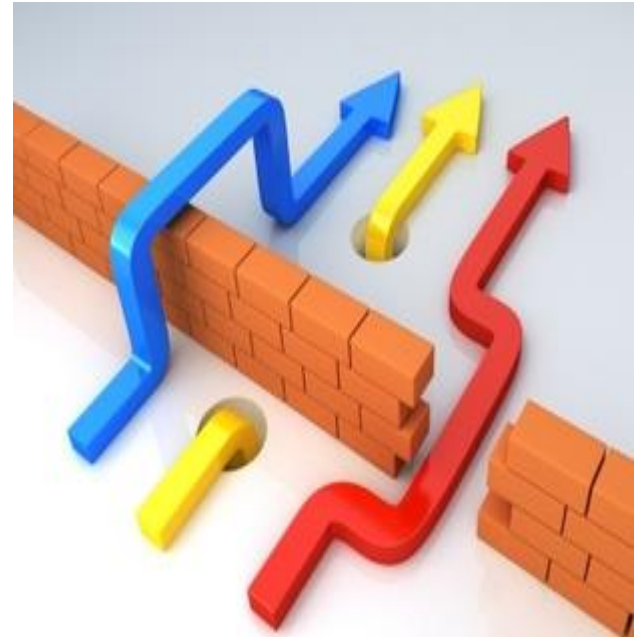
Merits

- Limited liability:
- Transfer of interest:
- Perpetual existence:
- Scope for expansion:
- Professional management:



Limitations

- Complexity in formation:
- Lack of secrecy:
- Impersonal work environment
- Numerous regulations:
- Delay in decision making:
- Oligarchic management
- Conflict in interests



Types of Companies

A company can be either a Private or a Public Company.

Difference between a Public Company and Private Company

Basis	Public company	Private company
Members	Minimum – 7 Maximum - unlimited	Minimum – 2 Maximum - 200
Minimum number of directors	Three	Two
Index of members	Compulsory	Not compulsory
Transfer of shares	No restriction	Restriction on transfer
Invitation to public to subscribe to shares	Can invite the public to subscribe to its shares or debentures	Cannot invite the public to subscribe to its securities

Private Company

A private company means a company which:

- (a) restricts the right of members to transfer its shares;
- (b) has a minimum of 2 and a maximum of 200 members, excluding the present and past employees;
- (c) does not invite public to subscribe to its securities and

It is necessary for a private company to use the word *private limited* after its name.

If a private company contravenes any of the aforesaid provisions, it ceases to be a private company and loses all the exemptions and privileges to which it is entitled.

privileges of a private limited company

1. A private company can be formed by only two members
2. There is no need to issue a prospectus
3. Allotment of shares can be done without receiving the minimum subscription.
4. A private limited company can start business as soon as it receives the certificate of incorporation.
5. A private company needs to have minimum two directors maximum fifteen.
6. A private company is not required to keep an index of members

Public Company

A public company means a company which is not a private company. As per The Companies Act, a public company is one which:

- (a) has a minimum of 7 members and no limit on maximum members;
- (b) has no restriction on transfer securities; and
- (c) is not prohibited from inviting the public to subscribe to its securities.

However, a private company which is a subsidiary of a public company is also treated as a public company.

CHOICE OF FORM OF BUSINESS ORGANISATION

After studying various forms of business organisations, it is evident that each form has certain advantages as well as disadvantages. It, therefore, becomes vital that certain basic considerations are kept in mind while choosing an appropriate form of organisation.

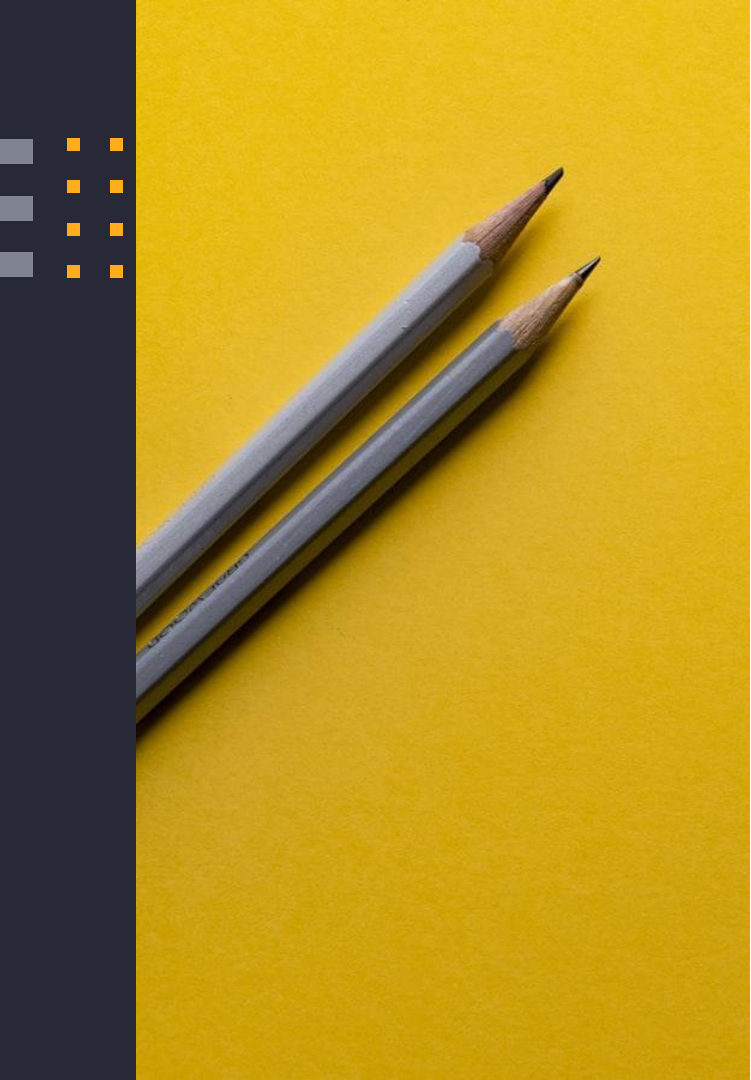


Factors influencing the choice of form of Business Organisation

- (i) Cost and ease in setting up the organisation: ,
- (ii) liability
- (iii) Continuity
- (iv) Management ability
- (v) Capital considerations
- (vi) Degree of control
- (vii) Nature of business
- (viii) risk

Factor	Form of organisation	
	Most advantageous	Least advantageous
Availability of capital	Company	Sole proprietorship
Cost of formation	Sole proprietorship	Company
Ease of formation	Sole proprietorship	Company
Transfer of ownership	Company (except private co)	Partnership
Managerial skills	Company	Sole proprietorship
Regulations	Sole proprietorship	Company
Flexibility	Sole proprietorship	Company
Continuity	Company	Sole proprietorship
Liability	Company	Sole proprietorship

Basis of comparison	Sole proprietorship	Partnership	Joint Hindu family business	Cooperative society	Company
Formation	Minimal legal formalities, easiest formation	Registration is optional, easy formation Less legal formalities,	exemption from registration, easy formation	Registration compulsory, greater legal formalities	Registration compulsory, lengthy and expensive formation process
Members	Only owner	Minimum-2 Maximum: 50	At least two persons for division of family property, no maximum limit	At least 10 adults, no maximum limit	Minimum Private-2 Public -7 Maximum Private -200 Public -unlimited
Capital contribution	Limited finance	Limited but more than that can be raised in case of sole proprietorship	Ancestral property	Limited	Large financial resources
Liability	Unlimited	Unlimited and joint	Unlimited (Karta), Limited (Other members)	Limited	Limited
Control and management	Owner takes all decisions, quick decision making	Partners take decisions, consent of all partners is needed	Karta takes decisions	Elected representative, i.e., managing committee takes decisions	Separation between ownership and management
Continuity	Unstable, business and owner regarded as one	More stable but affected by status of partners	Stable business, continues even if karta dies	Stable because of separate legal status	Stable because of separate legal status



Thanks!

