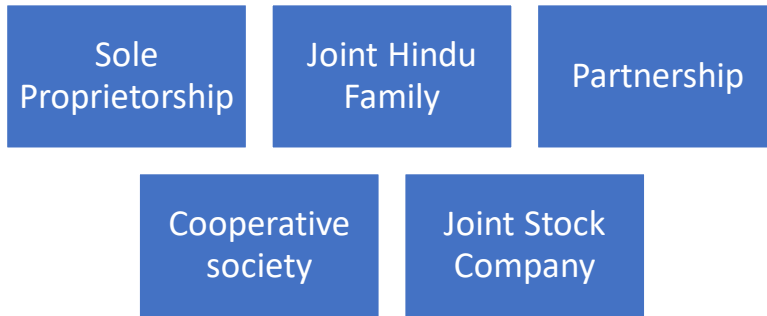


Class 11 Business Studies
Chapter 2 Forms of Business Organisation

Revision Notes

Forms of Business Organisation:



Sole Proprietorship : Meaning, Features, Merits and Limitation:

- 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

Features	Merits	Limitation
<ul style="list-style-type: none"> • There is no separate law to govern sole proprietorship • Owner is personally liable for payment of its debts i.e. he has unlimited liability • He is solely responsible for failure as well as profit • He has the right to run the business and make all decision • Business is not separate from owner i.e. business • Death, insanity, bankruptcy, physical ailment, imprisonment of sole proprietor will effect the continuity of business 	<ul style="list-style-type: none"> • Quick decision making as there is no need to consult others • Keep business operations confidential and maintain secrecy • Sole owner of the profit earned i.e. maximum incentive for hard work • Contributes to self satisfaction and sense of accomplishment • No separate law to govern sole proprietorship i.e. it is easy to start and close the business at his wish 	<ul style="list-style-type: none"> • Lack of resources (finance and borrowings) is a major drawback in the size and growth of the business • Death, insanity, imprisonment, physical ailment, bankruptcy affects the business and can lead to its closure • An unfavourable decision can create burden on the owner as his liability is unlimited • Decision making is not balanced as owner cannot excel in all managerial tasks

Joint Hindu Family

- form of organisation wherein the business is owned and carried
- by the members of the Hindu Undivided Family (HUF)
- basis of membership in the business is birth in a particular family and three successive generations can be members
- business is controlled by the head of the family who is the eldest member and is called karta.
- members have equal ownership right over the property of an ancestor and they are known as co-parceners.

Features	Merits	Limitations
<ul style="list-style-type: none"> • Business does not require any agreement as membership is by birth. • There should be at least two members in the family and ancestral property to be inherited by them • The liability of all members except the karta is limited to their share of co-parcenary property of the business. The karta has unlimited liability. • Karta controls the family business and his decision are binding to all • Business continues even after the death of karta, next eldest becomes karta • Minors are also member of the business 	<ul style="list-style-type: none"> • As karta has control over the business, conflicts among member or interference in decision making is avoided • Operation of business are not terminated and continuity of business is not at stake. • Liability of co-parceners is limited to their share and their risk is well defined and precise • As business is run by family , loyalty and cooperation is received from family members 	<ul style="list-style-type: none"> • Faces problem of limited capital as business is run on ancestral property which limits expansion of business • Karta has unlimited liability, his personal property is used to repay the debts • Dominance of karta may cause conflict amongst them and may breakdown the family unit.

Partnership

- 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

Features	Merits	Limitation
<ul style="list-style-type: none"> • It is governed by The Indian Partnership Act, 1932. Has existence with legal agreement governing relationship, sharing of profit and losses • Partners of firm have unlimited liability. partners are jointly liable to repay the debts and contribute in their proportion of share • Reward comes in the form of profits which are shared by the partners in an agreed ratio. However, they also share losses in the same ratio • Partner with mutual consent share responsibility of decision making and day to day control of activities • Lack of continuity due to death, retirement, insolvency or insanity of partner can bring partnership to end • With minimum 2 partner partnership can be formed • Business carried by all or any one of the partner acting for all 	<ul style="list-style-type: none"> • Partnership can be formed easily by an agreement between partner into a place to carry out business and share risks • Partner can oversee different function according to their expertise • the capital is contributed by no. of partner • Reduces anxiety, burden and stress on partner as risk is reduced by sharing between partner • A partnership firm is not legally required to publish its accounts and submit its reports. Hence it is able to maintain confidentiality of information relating to its operations. 	<ul style="list-style-type: none"> • The liability of partners is both joint and several which may prove to be a drawback for those partners who have greater personal wealth. • partnership firms face problems in expansion beyond a certain size as capital investment is not sufficient to support large scale operation • Lack of continuity due to death, retirement, insolvency or insanity of partner can bring partnership to end • difficult for any member of the public to ascertain the true financial status of a partnership firm.

Types of Partner

Type	Meaning	Capital Contribution	Management	Share in profit or Losses	Liability
Active Partner	Partners who take actual part in carrying out business of the firm on behalf of other partners	Contributes capital	Participates in management	Shares profit/losses	Unlimited liability
Sleeping Partner	Partners who do not take part in day to day activities of business	Contributes capital	Does not participate in management	Shares profit/losses	Unlimited liability
Secret Partner	Partner whose association with the firm is unknown to the general public	Contributes capital	Participate in management but secretly	Shares profit/losses	Unlimited liability
Nominal Partner	Partner who allows the use of his/her name by a firm	Does not contributes capital	Does not participate in management	Generally does not Shares profit/losses	Unlimited liability
Partner by estoppel	Partner who with his/her own initiative, conduct, behavior gives an impression to others that he/she is partner of the firm	Does not contributes capital	Does not participate in management	Does not Shares profit/losses	Unlimited liability
Partner by holding out	Partner who knowingly allows himself or herself to be represented as a partner in the firm	Does not contributes capital	Does not participate in management	Does not Shares profit/losses	Unlimited liability

Types of Partnership

On the basis of duration



- ☐ Partnership at will
 - 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
- ☐ 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

On the basis of Liability



- ☐ General Partnership
 - 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
- ☐ Limited Partnership
 - the liability of at least one partner is unlimited whereas the rest may have limited liability
 - 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.

Partnership Deed

- The written agreement which specifies the terms and conditions that govern the partnership is called the partnership deed.

The partnership deed generally includes the following aspect:

- 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

Procedure for firm registration:

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.

The consequences of non-registration of a firm 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.

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 at the hands of middlemen obsessed with the desire to earn greater profits
- The process of setting up a cooperative society is simple enough and at the most what is required is the consent of at least ten adult persons to form a society
- The capital of a society is raised from its members through issue of shares.
- The society acquires a distinct legal identity after its registration

Features

- The membership of a cooperative society is voluntary as person is free to join a cooperative society, and can also leave anytime as per his desire.
- The society can enter into contracts and hold property in its name, sue and be sued by others. It has separate identity.
- The liability of the members of a cooperative society is limited to the extent of the amount contributed by them as capital
- The power to take decisions lies in the hands of an elected managing committee.
- The cooperative society through its purpose lays emphasis on the values of mutual help and welfare. Hence, the motive of service dominates its working

Merits

- The principle of 'one man one vote' governs the cooperative society. Each member is entitled to equal voting rights.
- The liability of members of a cooperative society is limited to the extent of their capital contribution
- Death, bankruptcy or insanity of the members do not affect continuity of a cooperative society
- the focus is on elimination of middlemen, this helps in reducing costs. The customers or producers themselves are members of the society, and hence the risk of bad debts is lower.
- The cooperative society exemplifies the idea of democracy and hence finds support from the Government in the form of low taxes, subsidies, and low interest rates on loans
- The cooperative society can be started with a minimum of ten members. The registration procedure is simple involving a few legal formalities

Limitations

- Resources of a cooperative society consists of capital contributions of the members with limited means. The low rate of dividend offered on investment also acts as a deterrent
- Cooperative societies are unable to attract and employ expert managers because of their inability to pay them high salaries
- Open discussions in the meetings of members as well as disclosure obligations it is difficult to maintain secrecy about the operations of a cooperative society.
- Interference in the functioning of the cooperative organisation through the control exercised by the state cooperative departments negatively affects its freedom of operation
- Internal quarrels arising as a result of contrary viewpoints may lead to difficulties in decision making.

Types of Cooperative Societies

- Consumer's Cooperative Societies
 - formed to protect the interests of consumers
 - society aims at eliminating middlemen to achieve economy in operations
 - It purchases goods in bulk directly from the wholesalers and sells goods to the members
 - Profits are distributed on the basis of either their capital contributions to the society or purchases made by individual members.
- Producer's Cooperative Societies
 - set up to protect the interest of small producer
 - The members comprise of producers desirous of procuring inputs for production of goods to meet the demands of consumers
 - Profits are distributed on the basis of their contributions to the total pool of goods produced or sold by the society.
- Marketing Cooperative Societies
 - established to help small producers in selling their products.
 - The members consist of producers who wish to obtain reasonable prices for their output
 - It pools the output of individual members and performs marketing functions like transportation, warehousing, packaging, etc., to sell the output at the best possible price.
 - Profits are distributed according to each member's contribution
- Farmer's Cooperative Societies
 - protect the interests of farmers by providing better inputs at a reasonable cost
 - The members comprise farmers who wish to jointly take up farming activities
 - The aim is to gain the benefits of large scale farming and increase the productivity.
 - Improves the yield and returns to the farmers, but also solves the problems associated with the farming on fragmented land holdings
- Credit Cooperative Societies
 - established for providing easy credit on reasonable terms to the members.
 - 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.
- Cooperative Housing Societies
 - established to help people with limited income to construct houses at reasonable costs.

- The members of these societies consist of people who are desirous of procuring residential accommodation at lower costs.
- The aim is to solve the housing problems of the members by constructing houses and giving the option of paying in instalments

Joint Stock Company

- A company is an association of persons formed for carrying out business activities and has a legal status independent of its members.
- A company can be described as an artificial person having a separate legal entity, perpetual succession and a common seal
- 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

- A company is an artificial person. It is created by law and exists independent of its members
- A company acquires a separate legal identity. The law does not recognise the business and owners to be one and the same.
- The formation of a company is a time-consuming, expensive and complicated process. Incorporation of companies is compulsory
- It will only cease to exist when a specific procedure for its closure, called winding up, is completed. Members may come and members may go, but the company continues to exist.
- The management and control of the affairs of the company is undertaken by the Board of Directors, which appoints the top management for running of business
- The liability of the members is limited to the extent of the capital contributed by them in a company. The members can be asked to contribute to the loss only to the extent of the unpaid amount of share held by them
- A company may
- or may not have a common seal.
- The risk of losses in a company is borne by all the shareholders.

Merits

- The shareholders are liable to the extent of the amount unpaid on the shares held by them
- Share of a public limited company can be sold in the market and as such can be easily converted into cash in case the need arises. This avoids blockage of investment and presents the company as a favourable avenue for investment
- Existence of a company is not affected by the death, retirement, resignation, insolvency or insanity of its members as it has a separate entity from its members.
- Capital can be attracted from the public as well as through loans from banks and financial institutions. Thus there is greater scope for expansion
- Company can afford to pay higher salaries to specialists and professionals. It can, therefore, employ people who are experts in their area of specialisations

Limitation

- The formation of a company requires greater time, effort and extensive knowledge of legal requirements and the procedures involved
- Separation of ownership and management leads to lack of effort as well as personal involvement on the part of the officers of a company
- Information of company is provided to Registrar of companies time to time and hence information is available to general public
- The functioning of a company is subject to many legal provisions and compulsions. This reduces the freedom of operations of a company and takes away a lot of time, effort and money
- Communication as well as approval of various proposals to Top, middle and lower level management may cause delays not only in taking decisions but also in acting upon them.
- Board of Directors are representatives of the shareholders who are the owners. The owners have minimal influence in terms of controlling or running the business
- Various demands pose problems in managing the company as it often becomes difficult to satisfy such diverse interest

Difference Between Public company and Private company

Basis for Comparison	Public Company	Private Company
Meaning	A company which is owned and traded publicly	A company which is owned and traded privately
Minimum member	7	2
Maximum Member	Unlimited	200
Minimum Director	3	2
Suffix	Limited	Private Limited
Start of Business	After receiving certificate of incorporation and certificate of commencement of business	After receiving certificate of incorporation
Statutory Meeting	Compulsory	Optional
Issue of Prospectus/ Statement in lieu of Prospectus	Obligatory	Not required
Public Subscription	Allowed	Not allowed
Quorum at AGM	5 members must present in person	2 members must present in person
Transfer of shares	Free	Restricted

Choice of Form of Business Organization

Factors influencing form of organisation	Most advantage	Least advantage
Cost and ease in setting up of business	Sole Proprietorship	Company
Liability	Company	Sole Proprietorship
Continuity	Company	Sole Proprietorship
Management ability	Company	Sole Proprietorship
Capital Consideration	Company	Sole Proprietorship
Degree of control	Company (except private company)	Partnership
Nature of business: direct personal contact	Sole Proprietorship	Company
Regulations	Sole Proprietorship	Company
Flexibility	Sole Proprietorship	Company