FORMS OF BUSINESS ORGANIZATIONS

In its literal sense, a 'Business' means any activity that keeps a person busy. However, business in its wider sense includes all individuals and group activities, directed toward earning money and acquiring wealth through production and exchange of goods and/or services. It includes industry as well as commerce. From this point of view, all those activities in the field of trade, manufacturing, transport, banking, warehousing, insurance, packaging, advertising etc. whether undertaken by an individual or a group of individuals with the objective of earning profits fall under the head 'Business'.

The main aim of doing any business is to earn profit. However, organization of a business must comply with any of the approved legal forms that gives the organization a distinct status and also helps to determines its identity.

There are four distinct forms of business organizations:

i) Sole proprietorship
ii) Partnership
iii) Joint stock company
iv) Cooperative society

SOLE PROPRIETORSHIP:

It is the simplest form of business organization and is known as 'one man business'. In this form of business organization, one person is solely responsible for providing capital, for bearing the risk of the enterprise and also for day-to-day management of the business. In retail pharmacy business chemist shop) individual professional skim is essential. Therefore, this form of business is best suited to a sole proprietor.

Salient Features of Sole Proprietorship:

1) Sole proprietor has full authority over the affair of business. He has to act according to his ability and skill.
2) The proprietor has to arrange the necessary capital and assets which are essential to run its business smoothly.
3) The profit earned in the business entirely belongs to the proprietor. Similarly losses in the business are also to be borne by him.
4) The liability of one sole proprietor is unlimited.
5) No legal formalities are required to start the business, except in certain business, where legal formalities are required to be fulfilled. For example, to start a retail drug store, a licence is needed from the drug administration.
6) The ownership lies with one person only. There is no partnership or association. The proprietor and the business enterprise are one and the same.

Advantages:

1) It is most easily form of all forms of business organizations, since to legal formalities are necessary for setting up this type of business.
2) The incentive of greater profits and fear of losses induce the proprietor to work to the best of this ability as well as the capacity.
3) The secrecy of the business affairs can be maintained.
4) The sole proprietor is free to take any decision in regard to all matters concerning his business.
5) The sole proprietor is able to establish a personal contact with his customers.
6) Comparatively, there is little expenditure involved in managing the enterprise.
7) The sole proprietor is free to change the pattern of management at any time.
8) The capital investment in the business can be increased or decreased at will.
9) It encourages professionally qualified persons to set up their own business under self-employment scheme.

Disadvantages:

1) The individual proprietor generally suffers due to lack of adequate financial resources. As such, he usually finds it difficult to expand his business.
2) The business ends with the death of the proprietor because his heirs may not be as competent and qualified to run his business after his death.
3) It is very difficult for a single person to look after every aspect of the business viz., production, sale, finance, advertising and keeping the accounts competently.
4) The liability for business debts is unlimited.
5) There are no checks and controls on the sole proprietor.
6) The sole proprietor usually run his business only on a small sale. So he cannot enjoy the benefits of large-scale production or buying or selling. This may raise the cost of business operations.

JOINT HINDU FAMILY BUSINESS:

According to Mitakshara School of Hindu Law, the property which is inherited by a Hindu from his father, grandfather and great grandfather is ancestral property. Likewise, a son, his son and his son’s son become members of the Hindu joint family with co-owner or co-parcenary interest by virtue of being born in the family. The business is considered as part of the heritable property, the co-parcenary interest are also involved on the family business. A business which belongs to a single Hindu family and conduct it is a family business is called joint Hindu family business. The management and control of the family business is generally in the hands of the seniormost male member of the family who is known as the ‘Karta’. No legal formalities are required to convert a business into a joint family business. It automatically becomes so since on the death of the Karta, his legal male heirs inherit it.

Salient Features of Joint Hindu Family Business:

1) The membership of the family business is as a result of status arising from birth in the family. So there is no discrimination between any members in the family business.

2) Only the male members of the family can claim the right to be the member in the joint Hindu family business firm. The female members of the family cannot make any claim in this regard.
3) Only 'Karta' has the right to manage the family business.
4) The liability of all the members of joint Hindu family is limited, except 'Karta', who has unlimited liability.
5) The existence of the joint Hindu family business is not affected by the death or insolvency of a member or even Karta.
6) The share of each member of the family keeps on fluctuating. It increases on the death of any one of the existing co-parcener and decreases by birth of a new co-parcener.
7) The co-parcener can claim for its share or ask for the partition of the business if they are not satisfied with the functioning of the joint Hindu family firm.

Advantages:

1) Karta has full freedom run the business. He has the right to take decisions without any interference of others.
2) Every co-parcener get share in the profit of the business irrespective of his contribution in successful running of the business.
3) All the co-parceners have limited liability except 'Karta'.
4) The business has no effect of insanity or death of any member.
5) Thee business is just like insurance cover for children, widows, disable and sick members of the family.
6) The business can be run smoothly with the help of all the male members of the family.

Disadvantages:

1) Karta has unlimited authority to run the business. The initiative and sincerity of young members of the family has no place.
2) The resources of the joint family business are limited in comparison to other business organization.
3) The continuity of the joint Hindu family business depends upon the continuity of the joint Hindu family itself.
4) All the members has the right to get share in income and profits of business irrespective of their involvement of the business. This makes the members of the family irresponsible and lazy.

PARTNERSHIP:

The Indian Partnership Act defines partnership as a relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all. The persons who have entered into partnership are individually known as 'Partners' and collectively as a 'Partnership'. The business organization runs as a partnership is called as a 'Firm'.

Salient Features of Partnership:

1) In partnership business organization two or more persons, upto a maximum of twenty (ten in case of a banking firm) join together to share any profit made by the firm.
2) Partnership is formed in the basis of an agreement between the concerned persons. The partnership agreement may be oral, written or implied between the persons joining together in the partnership. The document containing the agreement is called the 'Partnership Deed'.
3) Any profit made by the partnership must be distributed among the partners in the agreed ratio, usually in proportion to the amount of capital invested by each partner in the firm.
4) A partner cannot transfer his share to an outsider without the consent of the other partner(s).
5) A partnership is dissolved automatically when the term for which the partnership was entered into expires or when a partner dies or retires.
6) If and when a partnership is dissolved, the firm does not, however, necessarily stand dissolved. It depends on the remaining partners whether to continue the firm. However, the dissolution of the firm take place in the following circumstances:
7) Each partner of the firm has unlimited liability. If the assets of the firm are sufficient to satisfy the claims of creditors of the firm, even the personal property of the partners can be attached to clear such claims.

Advantages:

1) A partnership is quite easily formed. Any two (or more) legally competent persons may start a business on partnership basis after executing an agreement between them which may be oral, written or implied.
2) Partnership may pool their individual resources to collect enough finance for smooth running of the business and also for its expansion as and when required.
3) Decision to start a partnership organization is quite prompt since partners can meet as and when needed.
4) There is a greater efficiency in day-to-day conduct of the business on account of personal interest taken by the partners in the management of the business.
5) A balance judgement is made regarding business issue avoiding individual preferences and prejudices.
6) Since any loss incurred by the firm is shared by all the partners, it reduces risk to the business as a whole.
7) A partnership firm has a longer existence because it is not depend on any one person.
8) The business can be expanded by extending the partnership provided the number of partners does not exceed twenty.
9) Since there is an unlimited liability of the partners, it serves as an important security to creditors who lend money to the firm.

Disadvantages:

1) It has been seen that in certain cases, it is difficult to maintain mutual understanding and harmony among the partners after the firm has worked for some time.
2) There is a lack of stability in the business. Death, insolvency or retirement of a partner may result in dissolution of the partnership.
3) A dishonest or incompetent partner may land the firm in difficulties because his acts would also bind the firm and remaining partners.
4) A partner who wants to withdraw his capital from the firm will not be able to do so unless all the other partners agree to it. This deprives a partner of the possibility of higher return on his capital elsewhere.
5) Partners bear an unlimited liability for the debts of the firm. Business creditors can recover their dues from all or any of the partners. In case the assets of the business are not enough for this purpose, the private property of the partners can be used to meet the liabilities of the firm.
6) A large scale business cannot generally be run on partnership basis because of the legal ceiling on the number of the partners and also due to limited resources of the partners.
7) Generally the public does not have much faith in partnership business, because the affairs of the partnership are kept a closely guarded secret and their business is not subject to Government control.

KINDS OF PARTNERS:

The partners of a firm may be divided into the following types:

i) Active or working partner: He takes an active part in the management of the firm's business and bears and unlimited liability for the debts of the firm. Like other partners, an active partner also contributes capital to the firm.

ii) Sleeping or inactive partner: A sleeping partner does not take any active part in the management of the firm's business. He, however, contributes capital and shares the profits/losses of the firm. His liability for the debts of the firm is unlimited.

iii) Nominal partner: He only leads his name to the firm as a partner. He, however, neither invest any capital, nor claims any share in the profits of the business. Though he does not take any part in the management of firm's business, he bears unlimited liability fer the incurred by the firm.

iv) Partner in profit only: He invests his capital only with a view to earn a share in profits of the firm and has no liability as regards to any losses suffered by the firm. His liability for the firm's debt is however, unlimited.

v) Secret partner: A partner who does not want the fact of his being a partner to be known to outsiders, is known as a secret partner.

vi) Minor partner: A partner below the age of 18 being a minor, does not enjoy the rights of a gull-fledged partner in a partnership firm since, in law, he is not competent to contact. However, the Indian Partnership Act allows a minor to be admitted as a partner provided all the other partners agree to it. A minor as a partner is entitled to a share in the profits and property of the firm. His liability for the firm's debts is, however, limited in proportion to his share in the profits and property of the firm. On

attaining majority, a minor partner has choice to continue as partner or not. If he does not give a public notice of his choice within six months, he will be treated as having decided to continue as a partener. After becoming a partner of the firm, his liability will become unlimited w.e.f. the date of his original admission to the partnership.

vii) **Partner by estoppel:** If an outsider behaves in such a fashion that he is mistaken as partner of the firm by third party, he will be held liable to all those third parties who extend credit to the firm on the assumption of his being a partner. Such a person is known as Partner by Estoppel because of his having behaved as a partner, he can not deny the liabilities attaching to the position of a partner.

In actual practice, a partner by estoppel is not a partner of the firm. He neither contributes any capital nor takes part in the management of the firm.

KINDS OF PARTNERSHIP:

From the point of view of liability of partners, a partnership may be of two types, namely:

i) General partnership
ii) Limited partnership

i) General partnership:

In a general partnership, the liability of every partner is unlimited. In case, the assets of the firm are not sufficient to pay off its liabilities, even the private property of the partners may be used to meet the undischarged liabilities. However, a minor partner is an exception, because his liability for the firm’s obligations is limited to the proportion of his share of profits and the capital. Each partner of a general partnership is entitled to participate in the management of the business, unless the partners themselves decide otherwise.

ii) Limited partnership:

The unlimited liability of partner is general partnership discourages investment of large sums in the firm. The limited partnership is a way out of this difficulty although it is not permitted under the Indian law. The main features of such a partnership are:

- A limited partnership consists of two classes of partners, namely ‘General partners’ with unlimited liabilities and ‘Special’ or ‘Limited partners’ with their liability limited to their capital contribution.
- A limited partner simply invests his money in the firm. Though he is not entitled to take part in the management of the business, he is allowed to inspect the books of the firms for his information.
- The death, lunacy or bankruptcy of a limited partner will not effect the existence of the firm in any way. As such, a limited partnership is more stable than a general partnership firm.
- A special partner can not withdraw any part of the capital contributed by him. If he does so, his liability on the portion so withdrawn becomes unlimited.

- A special partner can not assign his share to an outsider without the consent of the general partners.

Comparison between 'Sole Proprietorship' and 'Partnership Business'

Sr. No.	Sole Proprietorship Business	Partnership Business
(1)	A single person is the owner of the business.	Two or more persons, upto a maximum of twenty (ten in case of banking firm) can join together to run the business.
(2)	The business is managed and controlled by the proprietor.	The business is managed and controlled by the partners.
(3)	The capital investment is managed by the proprietor.	The capital is invested by the partners in agreed ratio.
(4)	The business is unstable. It ends with the death or insolvency of the proprietor.	The business is relatively more stable.
(5)	The liability for business debts is unlimited.	The liability for business debts is unlimited but it is shared by the all partners.
(6)	The profit earned in the business is entirely belongs to the proprietor.	The profit earned in the business is shared between partners in agreed ratio.
(7)	The sole proprietor is free to change pattern of management at any time.	It depends upon the consent of the partners.
(8)	The secrecy of the business affairs can be maintained.	The secrecy of the business is shared between the partners, which are generally not disclosed to the public.

JOINT STOCK COMPANY:

A company is governed by the Company Act and it has to follow various of the Act. Hence the company form of organization has to comply with various statutory requirements. The growing needs of modern industry and commerce could not be met by sole proprietorship or partnership. A joint stock company is a better method of mobilizing financial resources. A joint stock company is organized to carry on a large scale because its capital requirements and risk obligations are too burdensome- for a single individual or for a few individuals to bear themselves.

Salient features of a Joint Stock Company:

1) A company is an incorporated association. It comes into existence only after registration under the Company Act 1956.
2) The members of shareholders are the owners of the company. The business is run by the board of directors elected by members in the general body meeting of the company.
3) The capital requirement in a business is divided into shares of small denominations so that, would be investors can invest small or large sums of money as they desire.

4) The shareholder is always free to withdraw from the membership of a company by transferring his shares.
5) The liability of the members of a joint stock company is limited to the unpaid value of shares held by them.
6) A company is a legal person. Only the law can bring it to an end. Its life does not depend on the life of its members. The shares of a company may change several hands on the stock exchange, but life of the company remains unaffected by such change.
7) A company, not being a natural person, cannot sign documents for itself. The common seal with the name of the company engraved on it is, therefore, used as a substitute for its signatures.
8) A company can own, hold and dispose of property in its own name. its shareholders cannot claim to be private or joint owners of that property.
9) A company profits are taxed at a flat rate against slab rate charged for non-corporate bodies.

Advantages:

1) A joint stock company is able to collect a large amount od capital. It attracts a wide range of investors by giving them the option to invest small or large sums as they desire. Due to the large financial resources at its command, a company can organize, a business on a large scale and afford to expand it further.
2) The liabilities of the member of a company is limited to the nominal value of the shares held by them.
3) The joint stock company enjoys perpetual succession. Insolvency, insanity or death of its members has no effect on the existence of the company.
4) The shares of the company can be transferred without any difficulty. Moreover, the facility of easy convertibility of shares into cash serves as an incentive to the investors.
5) Since a company has large resources at its command it can afford to appoint well qualified and experienced persons to run its business. The effective management helps the company to earn increasing profits.
6) The management of the company is conducted on democratic principles. The company is managed by directors who are elected by shareholders. The major policy decisions are taken by shareholders and the directors have only to work within the frame work of those decisions.
7) The risk for each member is reduce because it is diffused and soread over several members of the company.
8) A company pays income tax at flat rates. This means on higher profits, it will have to bear lower tax-liability as compared to other.

Disadvantages:

1) The formation of a company is costly and time-consuming process. There are a number of formalities which are required to be complied with.

2) The company is not managed by proprietors (shareholders). In fact it is managed by directors and paid officials who have no personal interest and therefore there is no incentive for them to manage it more efficiently. Directors sometimes misuse their positions and serves their own personal ends ignoring the interest of the shareholders.
3) The company cannot take prompt decisions because of the time-lag between board meeting and the difficulty of getting the requisite quorum.
4) It is not difficult for an unscrupulous management to indulge in malpractices. Sometimes bogus companies are floated to cheat the investors of their hard earned money.
5) The persons controlling a company have large financial resources at their disposal. They may attempt to influence the economic and political decisions made by the Government.
6) The joint stock company when run on a large scale may gain exclusive control over production or distribution of a commodity. This may lead to exploitation of consumers by way of excessive pricing and poor quality of goods.
7) The secrecy of the business affairs cannot be maintained, because every issue is discussed in the meeting of boards of directors. The minutes of the meeting and accounts of the firm has to be notified.

KINDS OF COMPANIES:

Companies may be classified from four different points of view.

a) **From the point of view of incorporation:**
    1) Companies incorporated under a special chapter. This type of company does not exist in India.
    2) Companies established by a special act of parliament. These companies are also called statutory companies e.g. the Industrial Finance Corporation, LIC of India, Air India etc.
    3) Companies incorporated under the provisions of Company Act. These companies are also called registered Companies.
b) **From the point of view of liability:**
    1) Companies with unlimited liabilities
    2) Companies with liability limited by guarantee.
    3) Companies with liability limited by shares.
c) **From the point of view of nationality:**
    1) National companies i.e. those companies operate within the boundary of the country of registration.
    2) Multinational i.e. the companies which operate in various parts of the world.
d) **From the point of view of public interest:**
    1) Private company
    2) Public company
    3) Government company

- **Private Company:**

A company which is run by a minimum of two members or by maximum of fifty members, does not allow public subscription to its shares and it also restricts the transfer of its share, is called a private company. A private company combine in itself the advantage of limited liability with the facilities of the partnership organization. For this reason, it is preferred by many businessman. At the same time a private company is not as suitable a form of business organization as a partnership, because the firm will have to pay higher income-tax as compared to partnership organization. Moreover, the goodwill of the firm will be adversely affected by the limited liabilities of its partners.

- **Public Company:**

A company can be formed by a minimum of seven persons, having no maximum limit on its members, offers its shares to the public with a view to collect large sums of money to finance its projects and also does not restrict the right of its members to transfer their shares freely. Such a company is called 'public company'.

- **Government Company:**

A company is called a 'Government Company' if atleast 51 per cent of its share capital is held by the Central Government, a State Government or jointly by the Central Government and State Government.

Comparison between 'Joint Stock Company' & 'Partnership Firm'

Sr. No.	Joint Stock Company	Partnership Firm
(1)	The company is firmed by registration under Company Act 1956.	The partnership firm is formed by agreement among partners.
(2)	The registration of the company is compulsory.	The registration of the firm is voluntary.
(3)	The liability of the share-holders are limited to the extent of unpaid value of shares held by them.	The liability of the partners are unlimited jointly and separately.
(4)	The public limited company can be formed by a minim um of seven persons with no upper limit (private company is run by minimum of 2 members and maximum of 50 members)	The firm is formed with minimum of two and maximum of twenty members for general business (10 members for a banking business)
(5)	The shares of the company can be transferable.	A partner cannot transfer his share to an outsider without the consent of the other partners.
(6)	The resources of the company are unlimited. The huge amount of money can be raised by floating shares in the market.	The resources of the firm are limited. The capital of the firm can be raised only by the contribution by the partners of the firm.
(7)	The company is managed by board of directors.	The firm is managed by the partners.

(8)	The audit of the company's account is compulsory.	The audit of the firm's accounts is not compulsory.
(9)	There are number of restrictions imposed by the Government on the companies because they are governed by the Company act.	There are very limited control and regulation by the Government on the firms.

COOPERATIVE SOCIETY:

Cooperative organization is a voluntary association of persons who are financially strong. They come together with an aim not to get profits but to overcome destability arising out of want of adequate financial resources.

Salient Features of Cooperative Society:

1) A cooperative society is a voluntary organization made by association of persons and not of capital. There is no discrimination as regards the membership of the society. A member can withdraw from society after giving due notice to that effect.
2) The management of the affairs of society is in the hands of the managing committee which is elected by the members. The board polices are framed by the members and the management committee is required to perform its duties within its parameter. Each member is entitled to a single vote, irrespective of number of shares held.

$$Members \xrightarrow{Elect} Managing\ Committee \rightarrow Office\ Bearers \begin{bmatrix} President, \\ Vice\ President, \\ Secretary, \\ Treasurer \end{bmatrix}$$

3) The capital of a cooperative society is contributed by its members through purchase of shares. The cooperative society generally lay down a limit to the amount of capital which may be subscribed by an individual member. A cooperative society can also add to their capital resources by loans from the central and state cooperative banks.
4) The shares of the society cannot be transferred by members to others. In case a member wants to withdraw his capital, he has to return the shares.
5) In a cooperative society, distribution of profits is not related to the share capital contributed by each member. The main criterion is the value or volume of business transferred by each member with the cooperative society i.e. even with a small capital contribution, a member can receive a relatively large share in the profits if he has had a number of business transactions with the society.
6) A cooperative society conduct business on cash basis and does not allow credit facility.
7) A cooperative society is required to be registered under the Cooperative societies Act, 1912.
8) The surplus at the end of the year is not distributed as dividend among shareholders in the proportion to the share capital invested in the cooperative society. The share capital is treated as loan capital on which a moderate rate of interest is allowed out of net surplus. A portion of the balance is utilized for the general benefit of the members.

A portion may be paid as bonus to the employees and workers. The rest of net surplus is distributed among the members in proportion to their individual purchases from the society.

ADVANTAGES:

1) A cooperative society is voluntary association that may be formed by any 10 adults persons. Only a few legal formalities are required.
2) The liability of the members of a cooperative is limited to a certain proportion of their capital contribution in the society.
3) The life of a cooperative society is not affected by the death insolvency or conviction of a member.
4) The management of a cooperative is based on the principle of one-man one-vote. There is no discrimination on the basis of the number of shares held by members.
5) There is coordination among members of a cooperative society because they belong to a local area or a particular class or group and are inspired by the idea of cooperation.
6) The law governing the cooperative lays down the maximum limit as to the rate of interest on the capital contributed by each member. It also places a limit on the dividend to be declared as shares. The balance of the surplus earned in any year can be utilized for the growth and development as well as expansion of cooperative society.
7) The State Government offers many types of assistance, such as, facility of loans at much lower rate of interest. Moreover, they are granted several exemptions and reliefs besides low rate of tax.
8) The membership of cooperative society is open to everybody. There is no debar from joining the society on the basis of economic position, caste, colour or creed. There is no limit to the maximum number of members in running the cooperative society.

Disadvantages:

1) There is always shortage of capital for a cooperative society, because it generally has poor or lower middle class persons as its members. They can provide only a limited amount of capital.
2) A cooperative is managed by a managing committee which generally lacks technical knowledge and experience to run an undertaking. Hence, due to lack of proper management there is generally inefficiency in cooperatives.
3) The affairs of cooperatives are generally so much exposed to the members that it becomes difficult for them to maintain the business secrecy.
4) The excessive state regulation and control over the functioning of the cooperatives affects their working.
5) There is lack of motivation among the members of the managing committee because the rate of return to the members is limited by law.
6) Due to difference in opinion among the members, they may compete with one another to gain control over the affairs of the cooperative which may result in adverse consequences for the business of the cooperative.

STUDY QUESTIONS: