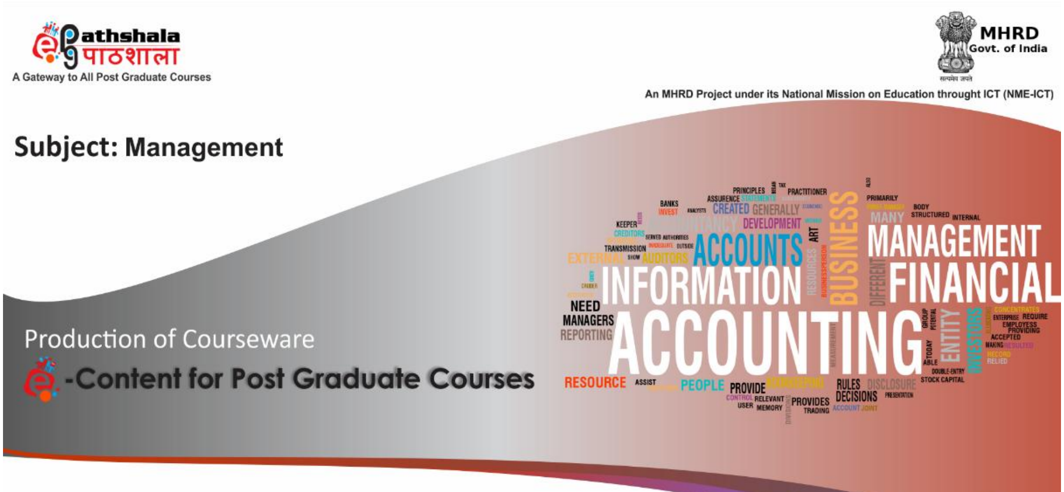

Paper: 09, Entrepreneurship Development and Project Management

Module: 16, Forms of Business Ownerships

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Items	Description of Module
Subject Name	Management
Paper Name	Entrepreneurship Development and Project Management
Module Title	Forms of Business Ownerships
Module Id	Module no.-16
Pre- Requisites	Basic knowledge of Business and Entrepreneurship
Objectives	To study the various forms of business ownerships
Keywords	Ownership, Sole trade, LLP, Company, Cooperatives

QUADRANT-I

Module 16:Forms of Business Ownerships
1. Learning Outcome
2. Introduction
3. Forms of Business Ownerships
4. Sole Trade
5. Joint Hindu Family Business
6. Partnership Firm
7. Limited Liability Partnership
8. Joint Stock Company
9. One Person Company
10. Cooperative Enterprise
11. Summary

You have studied in the earlier modules about entrepreneurship, entrepreneur, and enterprises. You are also aware about how to generate business idea and what are the different types of entrepreneurships? In this module you will learn about the various forms of business ownerships and what are the criteria on which you will evaluate the selection of particular form of business ownership.

1. Learning Outcome:

After studying this module the learners will be able to:

- Understand the various forms of business ownerships;
- Describe the various features of different forms of business ownerships;
- Explain the relative advantages and disadvantages of each form of business ownership;
- Understand the factors affecting choice of forms of business ownership; and
- Evaluate the different forms of business ownership.

2. Introduction

"The various forms of business ownership are as such children whose father is Economic Expediency and whose mother is the Law."

- L.H. Haney

To initiate any entrepreneurial activity, an entrepreneur has to select a form of business ownership. In other words, one of the first decisions that an entrepreneur has to take as owner is, how the enterprise should be structured or through which form of ownership it would operate? The forms of businesses are associated with ownership which determines the authority and responsibility of the owners. In practical, the forms of business ownerships are those legal forms according to which an enterprise/business is organised and run. Hence, the legal form of business ownership is called the form of business ownership. The other parties recognise an enterprise and its existence through its form. Choosing the appropriate form for any entrepreneurial activity is very crucial as the success of enterprise depend on the selection of form of business ownership. The form of business ownership defines the rights and liabilities of entrepreneur(s), control, life span, and financial structure, etc.

3. Forms of Business Ownerships

The above description indicates that an enterprise can be run through various forms/modes. Some businesses are operated and managed by a single person and some by many people. Beside this, some businesses are run in private sector, while others are in the public (government) sector, and some are in joint (public and private). Under entrepreneurship, an entrepreneur can run his enterprise in following forms:

i) Sole Proprietorship or Sole Trade
ii) Joint Hindu Family Business/Firm
iii) Partnership Firm
iv) Limited Liability Partnership (LLP)
v) Joint Stock Company (Public and Private)
vi) One Person Company
vii) Cooperative Society/Enterprises

Sole trade, Joint Hindu Family business, and partnership firm can be categorised as non-corporate and others (LLP, Joint Stock Company, One Person Company, and cooperative enterprise) can be categorised as corporate forms of ownerships. The basic difference between these two categories is legal formalities. Non- corporate form of business may be started without any legal formalities while corporate forms of business ownerships can be started and run only after completing legal formalities as prescribed under the governing laws of respective forms of business ownerships.

Business Ownership

Non-corporate forms

1. Sole Trade
2. Joint Hindu Family Business
3. Partnership Firm

Corporate Forms

1. LLP
2. Joint Stock Company
3. One Person Company
4. Cooperative Society

Let us now discuss each form of business ownership in detail along with their characteristics, merits, demerits and suitability.

4. Sole Proprietorship

Sole Proprietorship is one of the simplest, oldest and least expensiveforms of business ownership in the world of entrepreneurship. Most of the present day forms of business ownerships are the developed forms of sole proprietorship. It is also known as sole trade, individual business or single entrepreneurship. This is very popular form of business in India. Due to various features provided by this form of business ownership, it is regarded as best form of business ownership.

Sole trade business is established by a single individual. He invests the required amount in the business, manages the business himself, bears all business risks alone and gets all the profits. Due to these unique features, William R. Basset said that "The one man control is the best in the world if that one man is big enough to manage everything". The owner of the business is known as Sole Trader. This individual entrepreneur is fully responsible for all business debts and liabilities. Examples of this form of business ownership are kirana stores, local restaurant, and home-based businesses, etc. In this form of business, entrepreneur has unlimited liberty to run his business. Entrepreneur may select any type of business without meeting any legal formalities except those in which license may be required from the government bodies like health department, the municipal authority, or some other bodies.

4.1 Features of Sole Proprietorship

Following are the major features or characteristics of the sole trade form of business ownership:

i) Sole trader is the only owner of all the assets and resources of business.
ii) Sole trade business is one man show as owner has to take all the decisions.
iii) The liability of the owner is unlimited and if the debts of the business are not met from the assets of the business, his personal property can be utilized for this purpose.
iv) The profitsof the business totally belong to owner and losses are borne by owner only.
v) Single entrepreneur can select any trade as per his choice.
vi) All the information pertaining to business rests only with business entrepreneur.
vii) There is no separate identity of business and owner in this form, both are the one.

4.2 Benefits of Sole Proprietorship

Sole trade business provides some special advantage and due to these advantages this form of business is very popular:

i) It is very easy to start as there is no need to complete any legal formalities except those cases where license is must. Example, to start medical store, it is necessary to get license form health department.
ii) Quick decision making is another advantage of this form of business as one man manages all the business activity.
iii) Sole trader is free to change his business at any point of time as he is the only owner of business.
iv) No outsider can get the secret information of the business like profits, losses, customers and assets, etc. as every information rests with the owner only.
v) Direct motivation is there in this form of business as owner solely takes all the profits and bears all the losses and risks.
vi) Sole trader can maintain personal relations with customers to know more about their tastes, like and dislikes etc.
vii) It provides training to run medium and large scale business to individual owners
viii) It can be started with minimum investment.

4.3 Disadvantages of Sole Proprietorship

Along with the above advantages sole trade business suffers from following disadvantages:

i) The biggest disadvantage of this form of business is unlimited liability. Owner's personal property can also be utilized to meet the debts of the business.
ii) Due to individual ownership, limited capital and sources are available for business.
iii) Limited managerial support is available for this form of business as one man can never have all the managerial skills.
iv) Stability of business is always questionable as owner can close his business at any point of time. Moreover, death of owner also leads to closure of the enterprise.
v) Sometimes business suffers from losses due to individual and hasty decisions.
vi) It suits only for few businesses like shops, restaurants, and small businesses etc.

5. Joint Hindu Family Business/Firm

A business enterprise which is run by the group of people belonging to the same family is known as Joint Hindu Family Business. This form of business is operated according to Hindu Law, where all the family members including unmarried daughters and wives are the members of the business. In simple terms, Joint Hindu Family Business is that form of business which is carried by all the members of Joint Hindu Family under the control of *Mukhiy*a (Head of the family). Mukhiya or Manager is known as Karta and members are known as Co-parceners. This form of business ownership is based on the two facts:

1) **Coparcenary:** It means common ownership in the ancestral property. As per Coparcenary, an individual have a right in the family property and can ask for his/her share. This individual is known as Coparcener.
2) **Common Property**: According to Hindu Law, Joint Hindu Family possesses a common property which is used for the welfare of all the members of the family. Common property includes; ancestral property, property created through ancestral property and personal property treated as family property.

According to Hindu Law there are two community controlling Hindu families; **Mitakshara** and **Dayabhag**. Mitakshara is popular in the country except Assam, Bengal and Some parts of Orissa. Under this community, with the birth, a son gets rights in the ancestral property. Dayabhag community exists in Assam, Bengal, and some parts of the Orissa. Under this community, a son gets rights in the ancestral property only after the death of the father.

5.1 Characteristics of Joint Hindu Family Business

Following are the characteristics of Joint Hindu Family Business:

i) Joint Hindu Family Business is operated according to Hindu Law.
ii) This form of business is controlled and managed by Karta.
iii) The liability of all the members (coparceners) except Karta is limited up to the individual's interest in the ancestral property. The liability of the Karta is unlimited.
iv) This form of business is easy to start as there is no need of any registration.
v) Shares of the family members may increase or decrease with the birth of new member or death of existing member.
vi) This is more permanent form of business than sole trade as there is not effect of any death on the business.

6. Partnership Firm

To overcome the limitations of older forms of business ownerships like lack of capital, limited skills, etc., a new form of business is available i.e. partnership form of business ownership. Partnership form of

business ownership is that form in which two or more than two individuals willingly join together and start some lawful entrepreneurial activity. A partnership firm is an association of two or more persons who run business together for the objective of profit earning.
According to section 4 of the Indian Partnership Act, 1932, “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.” Based on this definition it can be said that partnership is a kind of agreement between two or more than two persons to run the business and divide the profits of the business. These persons are known as partners and their group is called firm and the name under which they run their business is known as name of the firm.

6.1 Features of Partnership Firm

Following are the characteristics/features of the partnership which is governed under the Indian Partnership Act, 1932:

i) To establish a business under partnership form, there is a need of two or more than two persons. The Partnership Act does not fix any limit on the number of partners but as per Companies Act the number of partners cannot be more than ten in banking business and twenty in any other business. If the number of partners reduces below two and more than ten or twenty, than business is declared illegal.

ii) The existence of partnership firm comes from contract between members and not from status. It is important to have a contract between partners to be a legal firm. The agreement/contract between partners is known as Partnership Deed.

iii) There must be an agreement between partners to share profit or loss as profit is the main motive of business.

iv) Each partner is responsible collectively or individually for all the liabilities of partnership. Hence, in partnership form of business ownership, liability of the partners is unlimited.

v) It is very easy to form a partnership firm as there is no legal binding on registration of firm. Agreement may be oral or written. If partners want to register their firm, the procedure is very simple.

vi) This form of business is flexible in nature, if partner want to change their business, it can be changed.

vii) Due to unlimited liability, partners put their whole heated efforts to run their business.

viii) Due to limited number of partners, partnership firm may not raise much capital as other forms like companies can generate.

ix) In partnership, a partner cannot transfer his interest/share in the firm to outsiders without the consent of all partners.

x) Future of partnership firm is always uncertain. It may come to an end on the death of any partner and insolvency of any partner, etc.

xi) This form of business is suitable for small scale businesses and for those which required less capital investment.

7. Limited Liability Partnership (LLP)

Limited Liability Partnership, popularly known as LLP, is world recognised form of business ownership. This form of ownership was introduced in India by an Act i.e. Limited Liability Partnership Act, 2008 which was notified on 31st March, 2009.This form of business ownership combines the advantages of both partnership and company form of business organisation. LLP form of business enables entrepreneurs to combine professional knowledge and entrepreneurial skills. LLP is an alternative to the traditional partnership which contains the limitations of unlimited liability and limited managerial skills, etc. This form of business ownership enables professional knowledge and skill to combine, organise, and operate entrepreneurial activity in an efficient manner.

7.1 Characteristics of Limited Liability Partnership

Following are the features of Limited Liability Partnership (LLP):

i) LLP is governed by the Limited Liability Partnership Act, 2008. Provisions of Partnership firm are not applicable to Limited Liability Partnership form of business.

ii) LLP is a separate legal entity. It is an artificial person being invisible, intangible having no body, mind, and soul. It exists in the eyes of law.

iii) As per LLP Act, 2008, there should be at least two partners to start entrepreneurial activity. There is no maximum limit on the number of partners. If at any point of time, number of members reduces below two and LLP carries its business operation more than six months, the partner who carries the business more than six months shall be personally liable for the liability of LLP for those obligations of LLP incurred during that period.

iv) It has perpetual succession. Any change in its partners shall not affect its existence like ordinary partnership firm. This form of business is more similar to company form of business.

v) The liability of partners in LLP is limited up to the capital contribution of the partners.

vi) LLP shall have at least two Designated Partners who are individuals and one of them shall be a resident of India. In case of an LLP in which all partners are body corporate, at least two nominees of such bodies shall act as Designated Partners.

vii) LLP is formed to carry out business or profession with a motive of profit earning and partners are free to manage the business directly, unlike shareholders.

viii) Provisions of Companies Act on National Company Law Tribunal, Designated Partner Identification Number (DPIN), and Registrar of Companies have been made applicable to Limited Liability Partnership. Central govt. may further notify the provisions of Companies Act to any LLP.

ix) In LLP, Designated Partner Identification Number is mandatory for Designated Partner of LLPs.

x) Formation of LLP is simple as compared to companies but not as easy as in case of sole trade and partnership.

xi) LLP Act 2008 provides flexibility to the LLP to manage and operate its business. Partner can decide the operations and ways of business.

xii) In LLP, it is easy to join or leave LLP and partners can transfer the ownership according to the provisions and terms of LLP agreement.

xiii) LLP can attract finance from private equity investors and financial institutions etc.

xiv) Numbers of statutory compliances in LLP are limited as compared to company form of business.

8. Joint Stock Company

To remove the limitations of above discussed form of business ownerships, entrepreneurs have the option of company form of business organisation. According to H.L. Haney, “A joint stock company is a voluntary association of individuals for profits, having a capital divided into transferable shares, the ownership of which is the condition of ownership.” Company form of business ownership is the group of people which is incorporated under the Companies Act 1956. Many people jointly invest capital in a company; therefore it is called Joint Stock Company. The capital of company is divided into transferable shares, which means share can be bought and sold. Liability of members is limited. Company is a separate legal entity and its business is run through Common Seal. Existence of company is continuous or perpetual and separate from its members. In simple words, shares of company are transferrable and life of company is not affected by the entry and exit of its shareholders.

8.1 Characteristics of a Company

Following are the main features of company form of business ownership:

i) A company is an incorporated or registered association/group of persons. Minimum seven persons required to form a Public Company while minimum two persons can form a Private Company.

ii) A Company is known as artificial person as it is created by law.

iii) A company is a separate legal entity and it is free from its shareholders. It can buy property in its name and can enter into agreements.

iv) It has a perpetual succession. Existence of company is not affected by the life of its member and that is why it is said that member may come and go but company goes on forever.

v) Due to separate legal entity, liability of its shareholders is limited to the nominal value of the shares subscribed by the shareholder.

vi) Company is an artificial person so as it cannot put its signature. Companies Act provides the right to use a common seal. Common seal is a special seal bearing the name of the company and is remains in the possession of its Secretary.

vii) To make any document legal, it is compulsory to have the common seal along with the signatures of atleast two directors.

viii) Actions or activities of a company are determined through two main documents i.e. Memorandum of Association and Article of Association. Company cannot go beyond these two documents.

ix) A company can raise huge amount of capital by issuing shares and debentures in the market.

x) Due to huge capital, a company can also utilize the services of experts like specialised managers and Company Secretary, etc.

xi) Unlike sole trade and partnership firm, risk is divided into number of shareholders.

xii) The formation of a company is a difficult and expensive task. So many formalities are required to complete before start of business.

xiii) Since a company is an incorporated/ registered body, it has to follow many provisions and rules of different Acts.

xiv) Company form of business organisation is very popular and suitable specially for large scale businesses.

xv) Winding up of the company is also very difficult and a very lengthy procedure has to be followed to wind up the company.

8.1 Types of Companies

Companies are divided into following two categories:

A) Private Company: According to Sec. 3(1) (iii) of the Companies Act, 1956, a private company means a company which through its Article of Association:

a. Restricts its members to transfer its shares;
b. Puts limit on number of members i.e. minimum two and maximum 50;
c. Restricts public to subscribe its shares and debentures;

d. Minimum paid-up capital of one lakh rupees (amount is subject to change from time to time);
e. Any other restriction imposed by govt. time to time through Company Act.

B) Public Company: According to Sec. 3(1)(iv) of the Companies Act, 1956, "Public Company means a company which is not private." It means a company which:

a. Does not restrict its members to transfer its shares;
b. Does not put limit on maximum number of its members;
c. Invites public to subscribe its shares and debentures;
d. Minimum paid-up capital of five lakhs rupees (amount of capital is subject to change from time to time);
e. Any other restriction imposed by govt. time to time through Company Act.

9. One Person Company (OPC)

The concept of One Person Company (OPC) is provided in the provisions of New Company Act, 2013. This form of business ownership provides the benefits of company form of business to an individual also. OPC is a company in which an individual holds the whole of the share capital with other members. As per provision of section 2(62) of the Company Act, 2013 "one person company means a company which has only one person as member." One Person Company can be formed by only a natural person who is an Indian citizen and resident of India.

9.1 Characteristics of a One Person Company

Following are the features of One Person Company:

i) OPC is an incorporated entity and it may be registered with one person.
ii) The liability of the sole shareholder shall be limited up to capital contribution unless business is not run in mala fide manner.
iii) One Person Company is managed by the owner or his representative.
iv) There should be atleast one director of OPC.
v) OPC will meet all the statutory requirements as prescribed in Companies Act.
vi) It provides opportunities to small entrepreneurs and professional like charted accountants, lawyers, doctors, etc. to enjoy the benefits of company form of business.
vii) Along with corporate entity, it provides advantages like quick decision making and business secrecy, etc.
viii) Due to one man control, life of OPC is uncertain.
ix) It suits to professional activities and small businesses.

10. Co-operative Enterprise

Cooperative enterprises is a voluntary association of group of persons who have joined together to promote their common interest. The basic difference between Cooperative enterprise and other forms of businesses is that along with business principles, it follows the principle of serving members of the enterprise. Cooperative enterprise is formed and registered under Cooperative Societies Act, 1912 or under the concerned State Cooperative Societies Acts. It works under the motto "one for all and all for one." Examples of this form of business ownership are agriculture cooperatives, marketing cooperatives, and consumer cooperatives, etc.

10.1 Features of Cooperative Enterprise

i) It is a voluntary association of persons belonging to homogeneous group.

ii) Membership of cooperative enterprise is open to all and there is no limitation on the number of members.
iii) It works for the common interest of all the members of the cooperative enterprise.
iv) The prime motive of the cooperative firm is service of members.
v) Members of the cooperative contribute capital in the form of shares.
vi) It is a separate legal entity and has perpetual life and is not affected by the entry and exit of members.
vii) Cooperative firm's profit is distributed among its members in the form of dividend.
viii) Members of the cooperative perform the managerial tasks in democratic manner.
ix) Liability of its members is limited to the capital contribution.
x) Most of the finance is contributed by state or central govt. to cooperative enterprises.
xi) Cooperative enterprise gets exemption from tax on their earnings.

11. Determinants of choice of form of business ownership

Although it is the sole decision of the entrepreneur to choose the form of ownership for his entrepreneurial activity but following are the factors that affect the choice of form of business ownership:

i) Nature of entrepreneurial activity
ii) Size of business
iii) Degree of control expected by entrepreneur
iv) Requirement of finance or capital
v) Legal formalities
vi) Ease of formation
vii) Extent of liability of entrepreneur
viii) Stability of business
ix) Secrecy of business information
x) Winding-up formalities

12. Summary

An entrepreneur has to select a form of business ownership to initiate his entrepreneurial activity. We have discussed various forms of business ownerships along with their distinct features. Suitability of form of business ownership is dependent on various factors like nature of business, expected control, liability of owner, and ease of formation, etc. No particular form is best in all cases and selection of a particular form is depends on entrepreneur choice. But once a type of form of business is selected than it is very difficult to change and choose a new form. So, this decision should be evaluated on above given parameters. If an entrepreneur wants to start a small business and financial requirement of business is small, sole trade and partnership forms are suitable but if size of business is large and financial requirement is also huge, company form of business is best. Before taking any decision on form of business ownership, entrepreneur must evaluate each and every aspect of business on their merits and demerits.