

SECTION 1

SOLE PROPRIETORSHIPS

TEXT SUMMARY

One of the first decisions entrepreneurs must make is what kind of business organization they will have. A **business organization** is an establishment formed to carry on commercial enterprise. The most common form of business organization is the sole proprietorship. A **sole proprietorship** is a business owned and run by one person. About 75 percent of all businesses in the United States are sole proprietorships. However, since most sole proprietorships are small, they account for only 6 percent of all United States sales. Your local bakery, barber shop, and bicycle repair shop are most likely sole proprietorships.

The biggest advantage of the sole proprietorship is that the owner gets to keep all profits after paying income taxes. Another advantage is that sole proprietorships are easy to start. They can usually be opened with a small amount of

paperwork and legal expense. Owners also have complete control of their businesses, and can respond quickly to changes in the marketplace.

The most important disadvantage of sole proprietorships is unlimited personal liability. **Liability** is the legal obligation to pay debts. If the business fails, the owner may have to sell personal property to cover those debts. Another disadvantage is that it may be hard for sole proprietors to find capital to expand their businesses. It may also be hard to find good employees. That is because many small businesses cannot afford **fringe benefits**, or payments to employees other than wages, such as paid vacation, retirement pay, and health insurance.

THE BIG IDEA

Sole proprietorships are the most common form of business in the United States. Owners have both full control and unlimited liability.

GRAPHIC SUMMARY: *Sole Proprietorships—Advantages and Disadvantages*

Advantages	Disadvantages
Ease of starting up	Lack of permanence
Full control	Unlimited liability
Sole receiver of profit	Limited access to resources and labor

Sole proprietorships offer owners the advantages and disadvantages that come with full control of a business.

REVIEW QUESTIONS

1. Explain why sole proprietorships generate only 6 percent of sales in the United States, yet are the most common form of business organization.
2. **Chart Skills** What are the disadvantages of a sole proprietorship?

TEXT SUMMARY

A **partnership** is a business organization owned by two or more persons. The partners must agree on how profits and responsibilities are divided. The most common type of partnership is a **general partnership**. Partners in a general partnership share equally in both responsibility and liability. Doctors, lawyers, accountants and other professionals often form general partnerships. In a **limited partnership** only one partner is required to be a general partner. That partner has control over the business, but unlimited personal liability for the firm's actions. Other partners contribute only money. A newer type of partnership is the **limited liability partnership (LLP)**. In this type of partnership all partners are limited partners and are

shielded from personal liability in certain situations.

One important advantage of a partnership is that the responsibility for the business may be shared. In a successful partnership, each partner brings different strengths and skills to the business. Each partner's **assets**, or money and other valuables, improve the firm's ability to borrow funds for operations or expansion. Another advantage of partnerships is that like sole proprietorships, they are easy to start.

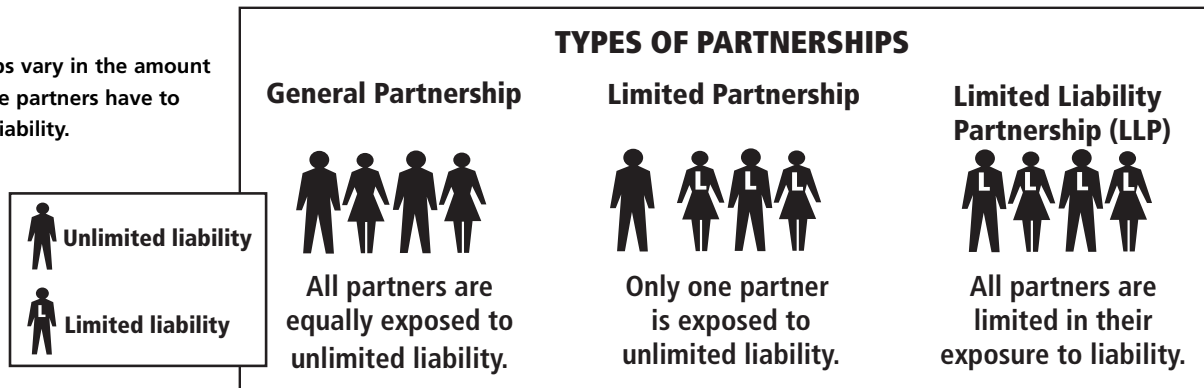
Partnerships also have disadvantages. Each general partner is responsible for the acts of the other partners. Unless the partnership is an LLP, at least one partner has unlimited liability. Like a sole proprietor, partners can lose their own personal property in paying the firm's debts. Another potential problem is conflict among the partners. They need to come to agreement about business goals and philosophies.

THE BIG IDEA

In partnerships, individuals pool their resources and share responsibility for running a business.

GRAPHIC SUMMARY: Partnerships and Liability

Partnerships vary in the amount of exposure partners have to unlimited liability.



REVIEW QUESTIONS

- How does a limited partnership differ from a general partnership?
- Diagram Skills** Which kind of partnership offers none of the partners protection from unlimited liability?

CORPORATIONS, MERGERS, AND MULTINATIONALS

TEXT SUMMARY

Most large businesses in the United States are corporations. A **corporation** is a legal entity, or being, owned by individual stockholders. Each stockholder has limited liability for the firm's debts, and can lose only as much as he or she has invested. Stockholders own **stocks**, which represent their share of ownership in the corporation. Like a person, a corporation pays taxes, can enter into contracts, and can bring lawsuits in court. All corporations have the same basic structure. Stockholders elect a board of directors. The board makes the important decisions for the corporation. It also appoints corporate officers who run the corporation.

The most important advantage of the corporate structure is limiting liability. Stockholders can only lose the amount of money they have invested. Corporations can raise money by selling stock on the stock market. Corporations

also borrow money by selling **bonds**. Bonds are certificates corporations issue, promising to repay the money they borrow with interest.

As a corporation grows, it may decide to merge, or combine, with another company or companies. **Horizontal mergers** join two or more firms in the same market. For example, two automakers may decide to form a larger company. **Vertical mergers** join two or more firms involved in different stages of making the same good or service. For example, an automaker may merge with the company that supplies it with rubber tires. **Conglomerates** combine companies which produce completely unrelated goods or services. **Multinational corporations (MNCs)** are corporations that operate in more than one country at a time.

THE BIG IDEA

Corporations are complex business organizations which offer limited liability to their owners, individual stockholders.

GRAPHIC SUMMARY: Corporations—Advantages and Disadvantages

ADVANTAGES	DISADVANTAGES
<ul style="list-style-type: none"> • As owners, stockholders have limited liability. • Corporation can sell stocks to raise money. • Corporations can borrow money by selling bonds. • Corporations can continue doing business after death of founders or owners. 	<ul style="list-style-type: none"> • Corporations pay a tax on income, and stockholders also pay personal income tax on payments made to them by corporations. • Corporations are difficult and expensive to start. • Founders may lose control of the company. • Managers and directors do not always act in the best interest of stockholders. • Corporations are subject to more government regulations than other kinds of businesses.

A major advantage of a corporation is that it protects its owners from liability.

REVIEW QUESTIONS

1. Who are the owners of a corporation?
2. **Chart Skills** What kinds of tax payments are associated with a corporation?

TEXT SUMMARY

A **business franchise** is a business that is semi-independent. It pays fees to a parent company. In return, the business gets the exclusive right to sell a certain product or service in a given area. The parent company, or franchiser, develops the products and business system and helps the local franchise owners produce and sell their products. For a small business owner, a franchise has the advantage of a built-in reputation. However, the franchise owner must give up some freedom, and must also pay fees and even a share of earnings.

A **cooperative** is a business organization owned and operated by a group of people for their shared benefit. **Consumer cooperatives** sell merchandise to their members at reduced prices.

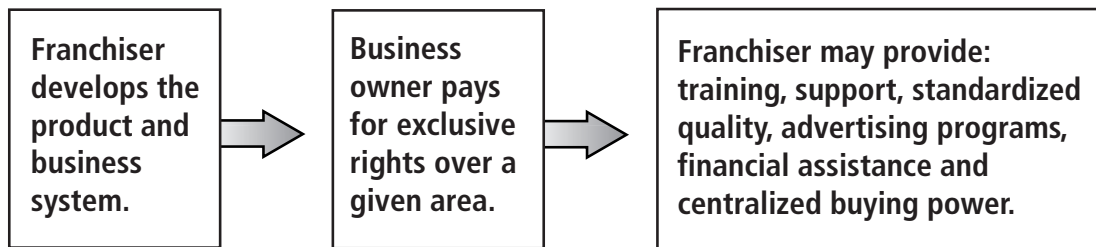
Cooperatives that provide a service rather than goods are called **service cooperatives**. Some service cooperatives offer discounted insurance, banking services, health care, legal help, or baby-sitting services. **Producer cooperatives** are agricultural marketing cooperatives that help members sell their products.

Nonprofit organizations function like businesses but do not operate for profit. These nonprofit organizations are usually in the business of serving society. Nonprofit organizations include museums, public schools, and YMCAs. The government exempts nonprofit organizations from income taxes. Many nonprofit organizations operate with partial government support. Nonprofit organizations that promote the interests of particular industries are called **trade associations**.

THE BIG IDEA

Different types of business organizations include franchises, cooperatives, and non-profit organizations.

GRAPHIC SUMMARY: *The Relationship between Franchiser and Business Owner*



A franchise owner gets support from a parent company that may include training, standardized quality, and national advertising, as well as a ready-made reputation.

REVIEW QUESTIONS

1. What is a cooperative?
2. **Diagram Skills** What does a business owner purchase when paying a fee to a franchiser?

CHAPTER 8**Test****IDENTIFYING MAIN IDEAS**

Write the letter of the correct answer in the blank provided. (10 points each)

- _____ 1. The most common form of business organization is
- A. the corporation.
 - B. the sole proprietorship.
 - C. the general partnership.
 - D. the franchise.
- _____ 2. Liability is the
- A. necessity to do a lot of paper work.
 - B. requirement to offer fringe benefits.
 - C. legal obligation to pay debts.
 - D. opportunity of the sole proprietor to keep all profits after taxes.
- _____ 3. A partnership is a business organization owned by
- A. one or more individuals.
 - B. two or more individuals.
 - C. individuals and stockholders.
 - D. one general partner and many stockholders.
- _____ 4. In a limited liability partnership, all partners
- A. always have no liability.
 - B. have personal liability.
 - C. are required to be general partners.
 - D. are limited from personal liability in certain situations.
- _____ 5. Most large businesses are
- A. sole proprietorships.
 - B. general partnerships.
 - C. corporations.
 - D. cooperatives.
- _____ 6. The most important decisions in a corporation are made by
- A. the investors.
 - B. the stockholders.
 - C. the board of directors.
 - D. the founders of the company.
- _____ 7. One of the ways a corporation can raise money is by
- A. selling stock on the stock market.
 - B. buying bonds from other corporations.
 - C. seeking money from the government for research and development.
 - D. selling shares to the founders.
- _____ 8. Which of the following is an example of a merger?
- A. An individual buys a franchise.
 - B. Two individuals form a partnership.
 - C. A company combines with a company that supplies it with raw materials.
 - D. A company sells bonds to raise money for expansion.
- _____ 9. In return for a fee to a franchiser, a business owner receives the right
- A. to sell the franchiser's stocks and bonds.
 - B. to run the business in the way he or she wishes.
 - C. to form a partnership with the franchiser.
 - D. to sell the franchiser's goods and services.
- _____ 10. Museums, public schools, and YMCAs are all
- A. exempt from paying income taxes.
 - B. completely supported by the government.
 - C. promoted by trade associations.
 - D. supported by professional organizations.