

# **BUSINESS ORGANIZATIONS LESSON**

Task: Please be sure to read the notes closely for understanding. If prompted to pause and watch a video, please do so and follow the instructions provided.

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## **NOTES**

Entrepreneurs must make many decisions as they start up new businesses. One of the first decisions they face is what form of business organization best serves their interest. A **business organization** is an establishment formed to carry on commercial enterprise. In other words, a business organization is a company, or firm.

## **SOLE PROPRIETORSHIPS**

A **sole proprietorship** is a business owned and managed by a single individual. That person earns all of the firm's profits and is responsible for all of the firm's debts. This type of firm is by far the most popular in the United States. According to the Internal Revenue Service (IRS), about 75 percent of all businesses are sole proprietorships. Most sole proprietorships are small, however. All together, they generate only about 6 percent of the all United States sales.

| <b><i>Advantages of Sole Proprietorships</i></b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | <b><i>Disadvantages of Sole Proprietorships</i></b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
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| <p><b><u>#1 Easy to Establish</u></b><br/>With just a small amount of paperwork and legal expense, just about anyone can start a sole proprietorship. To start a new business, a sole proprietor must meet a small number of requirements, which can vary from city to city, and state to state.</p> <p>Typically, sole proprietorships must meet the following requirements:</p> <ol style="list-style-type: none"><li>1. <i>Authorization</i> - a business license is needed from the local government.</li><li>2. <i>Site Permit</i> - if not operating out of the home, a building permit is needed.</li><li>3. <i>Name</i> - a business name must be chosen and registered</li></ol> | <p><b><u>#1 Unlimited Personal Liability</u></b><br/>There is unlimited personal liability. <b><i>Liability</i></b> is the legally bound obligation to pay debts. Sole proprietors are fully and personally responsible for all their business debts. If the business fails, the owner may have to sell personal property to cover any outstanding obligations.</p> <p><b><u>#2 Limited Access to Resources</u></b><br/>If your landscaping business takes off and grows quickly, for example, you might need to expand your business by buying more equipment. But, as a sole proprietor, you may have to expand by paying for the equipment out of your own pocket. This is because banks are sometimes unwilling to offer financing in the early days of a business. Many small business owners have</p> |

## **#2 Few Regulations**

A sole proprietorship is the least-regulated form of business organization. They are however, still subject to some government regulation and zoning laws.

1. *Sole Receiver of Profit* - the owner gets to keep all profits after paying income taxes.
2. *Full Control* - They can run their businesses as they wish. They can respond quickly to change in the marketplace, and they can take advantage of sudden opportunities.
3. *Easy to Discontinue* - If they decide to close their business, they can do so easily. They must pay all debts and other obligations like taxes, but they do not have to meet any other legal obligations to stop doing business.

already used their available savings and other personal resources to start up their businesses. This makes it difficult or impossible for them to expand quickly.

Physical capital is not the only thing in short supply. Human capital may be an issue too. A sole proprietor, no matter how ambitious, may lack some of the skills necessary to run a business successfully as times change.

Lastly, you may even have to turn down work because you simply don't have enough hours in the day or enough workers to keep up with demand.

## **#3 Lack of Permanence**

A sole proprietorship has a limited life. If a sole proprietor dies or closes shop due to retirement, illness, loss of interest in the business, or for any other reason, the business ceases to exist.

Sole proprietors also struggle to find and keep good employees. Small businesses cannot offer security and advancement opportunities that many employees look for in a job. Employers cannot offer *fringe benefits*, or payments to employees other than wages or salary (paid vacation, retirement pay, and health insurance).

**Please watch *Sole Proprietorship* (<https://www.youtube.com/watch?v=8eTFgRXc6WU>). Take notes on a separate Google Doc. Be sure to clearly label your work. Share it with me ([kwelgoss@wscschools.org](mailto:kwelgoss@wscschools.org)) upon the completion of the **WHOLE** assignment.**

## **PARTNERSHIPS**

A **partnership** is a business organization owned by two or more persons who agree on a specific division of responsibilities and profits. In the United States, partnerships account for about 7% of all businesses. They generate about 5% of all sales and about 10% of all income.

## Types of Partnerships

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| <b><u>General Partnership (GP)</u></b><br>The most common type of partnership in which partners share equally in both responsibility and liability. Many of the same kind of businesses that operate as sole proprietorships could operate as general partnerships. Doctors, lawyers, accountants, are some examples. | <b><u>Limited Partnership (LP)</u></b><br>In this partnership, only one partner can be a general partner. In other words, only one partner has unlimited personal liability for the firm's actions. The remaining partner or partners contribute only money. They do not actively manage the business. Limited partners can lose only the amount of their initial investment. A limited partnership must have at least one general partner, but may have any number of limited partners. The main advantage of being a general partner is having control of the business. The main drawback is the extent of liability. | <b><u>Limited Liability Partnership (LLP)</u></b><br>This is a newer type of partnership recognized by many states, in which all partners are limited partners. An LLP functions like a general partnership, except that all partners are limited from personal liability in certain situations, such as another partner's mistakes. Not all types of businesses are allowed to register as limited liability partnerships. Most states allow professionals such as attorneys, physicians, dentists, and accountants to register as LLPs. |
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There are several advantages and disadvantages to partnerships.

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| <b><u>Advantages of Partnerships</u></b><br><br><b><u>#1 Ease of Start Up</u></b><br>Partnerships are easy and inexpensive to establish. The law does not require a written partnership agreement. Most small business experts, however, advise partners to work with an attorney to develop <b><i>articles of partnership</i></b> , or a partnership agreement. This legal document spells out each partner's rights and responsibilities. It outlines how partners will share profits or losses. It may also address how new partners can join the firm, duration of the partnership, and tax responsibilities. If they do not have a partnership agreement, they will be protected under the <b><i>Uniform</i></b> | <b><u>Disadvantages of Partnerships</u></b><br><br><b><u>#1 Unlimited Liability</u></b><br>Unless the partnership is an LLP, at least one partner has unlimited liability. Any general partner could lose everything, including personal property, in paying the firm's debts. Limited partners do not face the same threat. They can lose only their investment.<br><br>In a partnership, each general partner is bound by the acts of all other general partners. For example, if one partner's actions cause the firm losses, then all of the general partners suffer. |
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**Partnership Act (UPA)**, a uniform state law adopted by most states to establish rules for partnerships. It requires common ownership interests, profit and loss sharing, and shared management responsibilities.

### **#2 Shared Decision Making and Specialization**

The responsibility for the business is shared. Each partner also brings different strengths and skills to business.

### **#3 Larger Pool of Capital**

Each partner's **assets**, or money and other valuables, improve the firm's ability to borrow funds for operations or expansion. In addition, larger firms have a greater ability to attract talented people, who are often drawn to the security of a larger firm.

### **#4 Taxation**

Partnerships are not subjected to any special taxes. Partners pay taxes on their share of the income that the partnership generates. The business itself, however, does not have to pay taxes.

### **#2 Potential for Conflict**

Partners are human and before they join together, they should talk about work habits, goals, management styles, ethics, and general business philosophies. Doing so, will avoid conflict that could lead to the break up of partnerships.

**Please watch Partnerships (<https://www.youtube.com/watch?v=5yGRpS8YKFI>). Take notes on a separate Google Doc. Be sure to clearly label your work. Share it with me ([kwelgoss@wscschools.org](mailto:kwelgoss@wscschools.org)) upon the completion of the WHOLE assignment.**

## **CORPORATIONS**

Businesses often rely on investment to expand operations. One way for a business to increase investment is to form a corporation. A **corporation** is a legal entity or being, owned by individual stockholders, each of whom faces limited liability for the firm's debts. Stockholders own **stock**, a certificate of ownership in a corporation. In other words, if you own a stock in a corporation, you are part-owner of that corporation. If a corporation issues 1,000 shares of stock, and you purchase 1 share, you own 1/1000th of the company.

A corporation is defined as an “entity” because it has a legal identity separate from those of its owners. Legally, it is regarded much like an individual. A corporation pays taxes, may engage in business, make contracts, sue other parties, and get sued by others.

In the U.S., corporations account for about 20% of all businesses, yet sell about 90% of all products sold in the nation. They generate about 70% of the net income earned in the nation. Some of the businesses that tend to incorporate are supermarkets, high-tech companies, and machinery manufacturers.

### **Types of Corporations**

| <b><i>Closely-held Corporations</i></b>                                                                                                                                                                                             | <b><i>Publicly-held Corporations</i></b>                                                                                                                                                                                                                                                                                                                      |
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| A type of corporation that issues stock to only a few people, often family members. These stockholders rarely trade their stock, and pass on the stock within families. They are also known as <i>privately-held corporations</i> . | A type of corporation that has many shareholders who can buy or sell stock on the open market. Stocks are bought and sold at financial markets called stock exchanges.                                                                                                                                                                                        |
|                                                                                                                                                                                                                                     | <b>Watch Stock Market Clip</b><br><a href="https://www.youtube.com/watch?v=p7HKvqRIBo">https://www.youtube.com/watch?v=p7HKvqRIBo</a><br><b>Take notes on a separate Google Doc. Be sure to clearly label your work. Share it with me (<a href="mailto:kwelgoss@wscschools.org">kwelgoss@wscschools.org</a>) upon the completion of the WHOLE assignment.</b> |

### **Advantages and Disadvantages of Corporations**

| <b><i><u>Advantages of Corporations</u></i></b>                                                                                                                                                                                                                                                                                                          | <b><i><u>Disadvantages of Corporations</u></i></b>                                                                                                                                                                                                                                                                                                                   |
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| <ul style="list-style-type: none"> <li>• Limited liability for owners</li> <li>• Transferable ownership</li> <li>• Ability to attract capital</li> <li>• Long life</li> </ul> <p><b><u>Advantages for Stockholders</u></b><br/>Investors do not carry responsibility for the corporation’s actions. They can lose only the amount of money they have</p> | <ul style="list-style-type: none"> <li>• Expense and difficulty of start-up</li> <li>• Double taxation</li> <li>• Potential loss of control by the founders</li> <li>• More legal requirements and regulations</li> </ul> <p><b><u>Difficulty/Expense of Start Up</u></b><br/>Charters to start a corporation can be difficult, expensive, and time consuming to</p> |

invested in the business. Shares of stocks are also transferrable, which means that stockholders can sell their stocks to others and get money in return.

#### Advantages for the Corporation

-Corporations have more potential for growth than other business forms. By selling shares on the stock market, corporations can raise money to purchase capital. A corporation can offer as many shares of stock as its corporate charter allows.

-Corporations can also raise money by borrowing it. They do this by selling bonds. A **bond** is a formal contract to repay borrowed money with interest at fixed intervals.

-Corporation owners (stockholders) do not need any special managerial skills. So, the corporation can hire various experts (financial analysts) to create and market the best services or goods possible.

-Corporations also have the advantage of long life. Stock is transferable, and therefore it can be bought and sold.

establish. Firms that want to incorporate must first file for a state license known as a ***certificate of incorporation***, or corporate charter. Once the state officials review and approve it, they grant a corporate charter and then the corporation may organize and sell a good or service.

#### Double Taxation

The law considers corporations legal entities separate from their owners. Corporations, therefore, must pay taxes on their income. Profit is a form of income. When stockholders receive income from the corporation in the form of ***dividends*** (the portion of the corporate profits paid out to the stockholders), the stockholders must pay personal income tax on those dividends. When stockholders sell their shares, they must pay a special tax, called a ***capital gains tax***, if they made a profit.

#### Loss of Control

The original owners of a corporation often lose control of the company. Managers and boards of directors, not owners, manage corporations. These managers do not always act in the owners' best interests.

#### More Regulations

Corporations must hold annual meetings for shareholders and keep careful records of all business transactions. Publicly-held corporations are required to file quarterly and annual reports to the Security and Exchange Commission (SEC). The SEC is a federal regulatory agency that regulates the stock market.

## MERGERS

As corporations continue to grow, managers and owners may decide it makes sense to merge, or combine, the firm with another company or companies. The three kinds of

mergers are **horizontal mergers**, **vertical mergers**, and **conglomerates**. Each of these corporate combinations can lead to larger, more efficient firms.

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| <p><u><b>Horizontal Mergers</b></u><br/>Horizontal mergers join two or more firms competing in the same market with the same good or service. For example, in 1998, two giant automakers, Chrysler Corporation and Daimler-Benz merged to reduce costs and boost revenues.</p> | <p><u><b>Vertical Mergers</b></u><br/>Vertical mergers join two or more firms involved in a different stage of producing the same good or service. It can allow a firm to operate more efficiently by allowing control of all phases of production, rather than relying on the goods or services of outside suppliers. A hypothetical example would be if a grocery store that sells milk and cheese, purchased a dairy farm that produces milk and cheese.</p> | <p><u><b>Conglomerates</b></u><br/>When firms buy other companies that produce totally unrelated goods or services. No one business earns the majority of the firm's profits.</p> |
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## **MULTINATIONAL CORPORATIONS**

The world's largest corporations produce and sell their goods and services throughout the world. They are called **multinational corporations (MNCs)**. MNCs are corporations that operate in more than one country at a time. They usually have headquarters in one country and branches in other countries. MNCs, which are sometimes called transnational corporations, must obey the laws and pay taxes in each country in which they operate. They account for more than \$3 trillion of worldwide assets, and often have operating budgets larger than most governments' budgets. Examples of MNCs include Microsoft, General Electric, Google, etc.

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| <p><u><b>Advantages of MNCs</b></u></p> <ul style="list-style-type: none"> <li>• Provide jobs and products around the world</li> <li>• Spread new technologies and production methods across the globe</li> <li>• Often help poorer nations gain better living standards for their people</li> </ul> | <p><u><b>Disadvantages of MNCs</b></u></p> <ul style="list-style-type: none"> <li>• May negatively influence the culture and politics in countries in which they operate</li> <li>• Pay low wages and tend to have firms with poor working conditions</li> </ul> |
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**Watch MNC Clip** (<https://www.youtube.com/watch?v=-rgLDwg1WsY>).

## **BUSINESS FRANCHISES**

A **business franchise** is a semi-independent business that pays fees to a parent company. In return, the business is granted the exclusive right to sell a certain product or service in a given area. Parent companies are called franchisers. The franchiser develops the products

and business systems. They then work with the local franchise owners to help them produce and sell their products. Many fast-food restaurants are franchises (McDonalds, Subway, Wendy's, etc.).

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| <p><b><i>Advantages of Franchises</i></b></p> <ul style="list-style-type: none"> <li>• The business comes in with a built-in reputation</li> <li>• Parent company provides training and support</li> <li>• There is standardized quality</li> <li>• Parent company does all advertising (national advertising)</li> <li>• Financial assistance from parent company is available for some franchises</li> <li>• Parent company buys in bulk and passes the savings down to the franchise</li> </ul> | <p><b><i>Disadvantages of Franchises</i></b></p> <ul style="list-style-type: none"> <li>• Franchise owner must sacrifice some freedom in return for the parent company's guidance</li> <li>• High franchising fees and royalties owed to parent company</li> <li>• Strict operating standards (hours of operation, dress code, operating procedures)</li> <li>• Purchasing restrictions (franchises must buy from the parent company or from approved suppliers)</li> <li>• Limited product line (only approved products can be offered)</li> </ul> |
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**Watch McDonalds Franchise Clip** ([https://www.youtube.com/watch?v=kr\\_iqkRcLHU](https://www.youtube.com/watch?v=kr_iqkRcLHU)).

## COOPERATIVES

A **cooperative** is a business organization owned and operated by a group of individuals for their shared benefit. Working together, the individuals can provide themselves with certain advantages. Cooperatives, or co-ops, fall into three main categories:

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| <p><b><u>Consumer Cooperatives</u></b></p> <p>These cooperatives sell merchandise to their members at reduced prices. By making large purchases, consumer cooperatives can obtain goods at a lower cost. They then pass the savings on to members. Examples include Sam's Club or BJ's Wholesale Club.</p> | <p><b><u>Service Cooperatives</u></b></p> <p>These cooperatives provide a service, rather than goods. They may offer discounted insurance, banking services, health care, legal help, etc. Examples include Credit Unions.</p> | <p><b><u>Producer Cooperatives</u></b></p> <p>These cooperatives are agricultural marketing cooperatives that help members sell their products. They allow members to focus their attention on growing their crops or raising their livestock. Examples include Dairy Co-ops.</p> |
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**Watch the Cooperative Clip** (<https://www.youtube.com/watch?v=8RCZPrUIU0o>).

## NONPROFIT ORGANIZATIONS

Some institutions function much like business organizations, but do not operate for the purpose of generating profits. These **nonprofit organizations** are usually in the business of benefiting society. Nonprofit organizations include museums, public schools, the

American Red Cross, hospitals, adoption agencies, churches, synagogues, YMCAs, and many other groups.

The government exempts non profit organizations from income taxes. Many operate with partial government support. Almost all provide services rather than goods.

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***Instructions: Please study these notes. Upon completion, take the following assessment for this Unit. Clearly label and place your answers in a Google Doc and share them with me ([kwelgoss@wscschools.org](mailto:kwelgoss@wscschools.org)).***

### **Assessment**

1. What is a business organization?
2. What is a sole proprietorship?
3. Identify and describe one advantage and one disadvantage of a sole proprietorship.
4. What is a partnership?
5. Describe the difference between a GP, LP, and LLP.
6. Identify and describe one advantage and one disadvantage of a partnership.
7. What is a corporation?
8. How does ownership of stock help the corporation?
9. Identify and describe one advantage and one disadvantage of a corporation.
10. What are dividends?
11. What is a merger?
12. Identify and describe the three types of mergers.
13. What is an MNC?
14. Identify and describe one advantage and one disadvantage of an MNC.
15. What is a business franchise?
16. Identify and describe one advantage and one disadvantage of a business franchise.
17. What is a cooperative?
18. What is the difference between a consumer, service, and producer cooperative?
19. What is a non-profit organization?
20. What is one advantage of being a nonprofit organization?