

## Forms of Ownership

BA291

### Learning Objectives

1. Define sole proprietorship and explain the six advantages and six disadvantages of this ownership model
2. Define partnership and explain the six advantages and three disadvantages of this ownership model
3. Define corporation and explain the four advantages and six disadvantages of this ownership model
4. Explain the concept of corporate governance and identify the three groups responsible for ensuring good governance
5. Identify the potential advantages of pursuing mergers and acquisitions as a growth strategy, along with the potential difficulties and risks.
6. Define strategic alliance and joint venture, and explain why a company would choose these options over a merger or an acquisition.

2

## Selecting Form of Organization

One of the first decisions that the business owner will have to make is how the business should be structured. All businesses must adopt some legal configuration that defines the rights and liabilities of participants in the business's ownership, control, personal liability, life span, and financial structure.

- Vision regarding the size and nature of the business.
- The level of control
- The level of "structure".
- The business's vulnerability to lawsuits.
- Tax implications of the different organizational structures.
- Expected profit (or loss) of the business.
- Ability to raise fund

3

## Forms of Business Ownership

| Structure                  | Control                                                                                                                                                                                                                                                                                                                            | Profits and Taxation                                                                                                                                                              | Liability Exposure                                                                                                                              | Ease of Establishment                                                                                         |
|----------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------|
| <b>Sole proprietorship</b> | One owner has complete control                                                                                                                                                                                                                                                                                                     | Profits and losses flow directly to the owners and are taxed at individual rates                                                                                                  | Owner has unlimited personal liability for the business's financial obligations                                                                 | Easy to set up; typically requires just a business license and a form to register the company name            |
| <b>General partnership</b> | Two or more owners; each partner is entitled to equal control unless agreement specifies otherwise                                                                                                                                                                                                                                 | Profits and losses flow directly to the partners and are taxed at individual rates; partners share income and losses equally unless the partnership agreement specifies otherwise | All partners have unlimited liability, meaning their personal assets are at risk for mistakes made by others partners                           | Easy to set up; partnership agreement not required but strongly recommended                                   |
| <b>Limited partnership</b> | Two or more owners; one or more general partners manage the business; limited partners don't participate in the management                                                                                                                                                                                                         | Same as for general partnership                                                                                                                                                   | Limited partners have limited liability (making them liable only for the amount of their investment); general partners have unlimited liability | Same as for general partnership                                                                               |
| <b>Corporation</b>         | Unlimited number of shareholders; no limits on stock classes or voting arrangements; ownership and management of the business are separate (shareholders in public corporations are not involved in management decisions; in private or closely held corporations, owners are more likely to participate in managing the business) | Profits are taxed at corporate rates; profits are taxed again at individual rates when (or if) they are distributed to investors as dividends                                     | Investor's liability is limited to the amount of his or her investment                                                                          | More complicated and expensive to establish than a sole proprietorship; requirements vary from state to state |

## Important Terms

### Unlimited liability

A legal condition under which any damages or debts incurred by a business are the owner's personal responsibility

### Limited liability

A legal condition in which the maximum amount each owner is liable for is equal to whatever amount each invested in the business

### Double taxation

Income taxes paid twice on the same source of earned income e.g. when income is taxed at both the corporate level and personal level.

### Limited life

End upon the withdrawal or death of an owner(s)

### Liquidity

A measure of how easily and quickly an asset such as corporate stock can be converted into cash by selling it

5

## Sole Proprietorships

### A business owned by a single person

- Consists of one individual doing business
- The simplest and most common structure chosen to start a business
- The most numerous form of business organization worldwide
- Owner is entitled to all profits and responsible for all business's debts, losses and liabilities



6

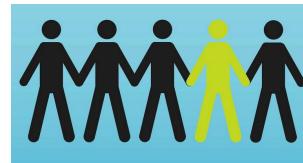
## Partnerships

A company that is owned by two or more people but is not a corporation

- Appropriate for firms that need more resources and leadership talent than a sole proprietorship but don't need the fundraising capabilities

### General partnership

All of the partners have the ability to actively manage or control the business. This means that every owner has authority to make decisions about how the business is run as well as the authority to make legally binding decisions.



7

## Partnerships (cont.)

### Limited partnership

A type of partnership that consists of at least one general partner and at least one limited partner

- General partners can be personally liable for all the partnerships' debts
- Limited partners are not liable for the partnership's debts beyond the funds they contribute to the partnership and does not participate in making managerial decisions for the business
- Limited partners receive proceeds from the business after the general partners have received their share of company profits

8

## Partnerships (cont.)

### Limited Liability Partnership (LLP)

A partnership in which each partner has unlimited liability only for his or her own actions and at least some degree of limited liability for the partnership as a whole

LLP does not have a general partner, since every partner in an LLP is given the ability to take part in the management of the company

Partners in an LLP have limited liability protection against malpractice suits that stem from another partner's negligent acts thus become popular in certain professions such as law, medicine and accounting

- All partners have limited liability protection against company obligations and debts
- Each partner receives profits and losses from the company according to her ownership interest in the company.

9

## The Partnership Agreement

A **partnership agreement** should address investment percentages, profit-sharing percentages, management responsibilities and other expectations of each owner, decision-making strategies, succession and exit strategies, and dispute-resolution procedures.



10

## Corporations

A **legal entity**, *distinct from any individual persons*, that has the power to own property and conduct business

- An independent legal entity owned by shareholders (investors who purchase shares of stock in a corporation)
- Corporation itself, not the shareholders that own it, is held legally liable for the actions and debts the business incurs
- Unlimited number of shareholders
- Private vs. Public



11

## Private vs. Public Corporation

### Private corporation

A corporation in which all the stock is owned by only a few individuals or companies and is not made available for purchase by the public

### “Privately Held”



### Public corporation

A corporation in which stock is sold to anyone who has the means to buy it

### “Publicly Traded”

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162.50 THB ▲0.50 (0.31%)



12

## Advantages vs. disadvantages

|                            | Advantages                                                                                                                                                                                                                                                                                          | Disadvantages                                                                                                                                                                                                  |
|----------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Sole Proprietorship</b> | <ul style="list-style-type: none"> <li>▲ Ease of formation / dissolution</li> <li>▲ Low start-up cost</li> <li>▲ In complete control of the business</li> <li>▲ Owner receives 100% of profit</li> <li>▲ Fewer regulations</li> <li>▲ No corporate income tax (single layer of taxation)</li> </ul> | <ul style="list-style-type: none"> <li>▼ Unlimited liability</li> <li>▼ Limited life (owner dies, the business dies)</li> <li>▼ Limited access to capital</li> <li>▼ Limited managerial perspective</li> </ul> |
| <b>Partnership</b>         | <ul style="list-style-type: none"> <li>▲ Ease of formation</li> <li>▲ Fewer regulations than corporation</li> <li>▲ Access to capital</li> <li>▲ Benefit from partners skills</li> <li>▲ No corporate income tax</li> </ul>                                                                         | <ul style="list-style-type: none"> <li>▼ Unlimited liability (except for Liability Limited Partnership)</li> <li>▼ Limited life (owner dies, the business dies)</li> <li>▼ Share control and profit</li> </ul> |
| <b>Corporation</b>         | <ul style="list-style-type: none"> <li>▲ Limited liability</li> <li>▲ Unlimited life</li> <li>▲ Transfer of ownership</li> <li>▲ Access to capital</li> <li>▲ Liquidity (public company)</li> </ul>                                                                                                 | <ul style="list-style-type: none"> <li>▼ Regulatory restrictions</li> <li>▼ Double taxation</li> <li>▼ More expensive to create than partnership or sole proprietorship</li> </ul>                             |

13

## Practice

Which one between sole proprietorship and partnership is treated as a separate legal entity? How do sole proprietor and partnership pay taxes?

14

## Practice

A and B agree to form a partnership. One day B died and John, B's son, told A that from now he will be a new general partner of this partnership. Do you agree with John? Will he be able to take B's role as a general partner to this partnership? Why?

15

## Practice

A and B, investing \$500,000 each equally, started a corporation called AB Corp. After 6 months of its operation, TU Corp sued AB Corp for breach of contract and the court ordered AB Corp to pay TU Corp \$5MM for damages. How much does A owe TU Corp?

16

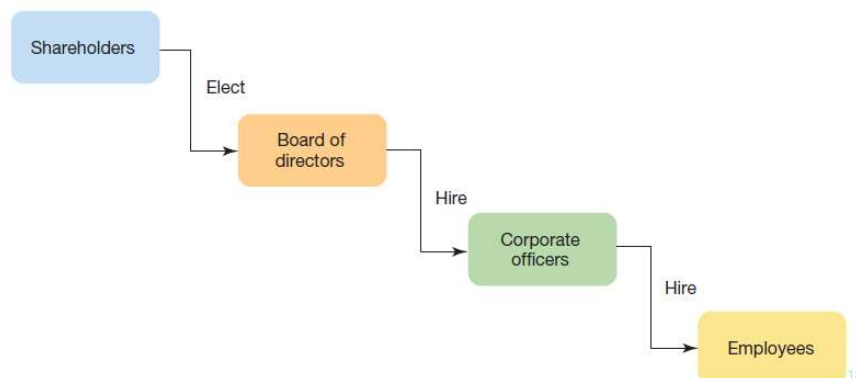
## Practice

A, B, and C agree to form a partnership, in which A will be general partner while B and C will be limited partners. The partnership borrowed \$1MM from Bangkok bank. The business did not perform well, so they decided to shut it down. Bangkok bank asked the partnership to pay back its loan of \$1MM. Who will be liable for the debt of \$1MM and why?

17

## Corporate Governance

- Describes all the policies, procedures, relationships, and systems in place to oversee the successful and legal operation of the enterprise
- Also refers to the responsibilities and performance of the board of directors specifically



18

## Corporate Governance

### Board of directors

A group of professionals elected by shareholders as their representatives, with responsibility for the overall direction of the company and the selection of top executives

19

## Mergers and Acquisitions

### Merger

An action taken by two companies to combine and perform as a single entity

### Acquisition

An action taken by one company to buy a controlling interest in the voting stock of another company

20

## M&A

### Hostile takeover

Acquisition of another company against the wishes of management

### Leveraged buyout (LBO)

Acquisition of a company's publicly traded stock, using funds that are primarily borrowed, usually with the intent of using some of the acquired assets to pay back the loans used to acquire the company

21

## Advantages of Mergers and Acquisitions

- Increase their buying power as a result of their larger size
- Increase revenue by cross-selling products to each other's customers
- Increase market share by combining product lines
- Gain access to new expertise, systems, and teams of employees

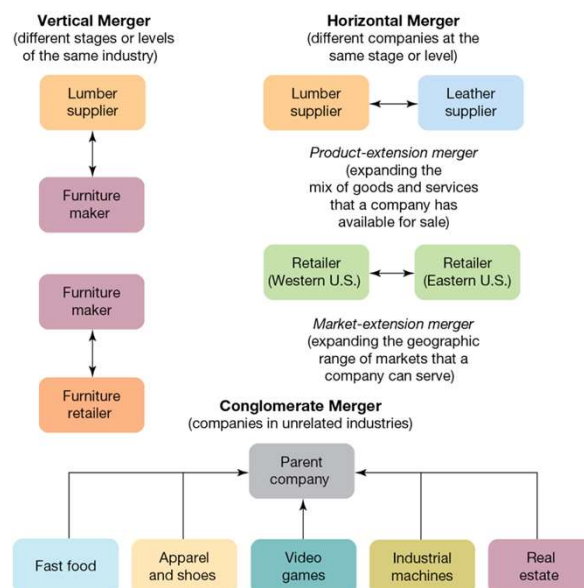
22

## Disadvantages of Mergers and Acquisitions

- Executives have to agree on how the merger will be financed.
- Managers need to decide who will be in charge after they join forces.
- Marketing departments need to figure out how to blend product lines, branding strategies, and advertising and sales efforts.
- Companies must often deal with layoffs.

23

## Types of Mergers



24

## Strategic Alliances and Joint Ventures

### Strategic alliance

A long-term partnership between companies to jointly develop, produce, or sell products

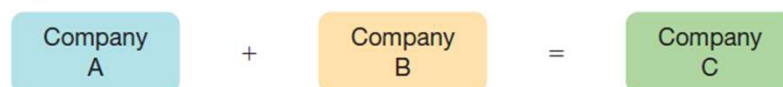
### Joint venture

A separate legal entity established by two or more companies to pursue shared business objectives

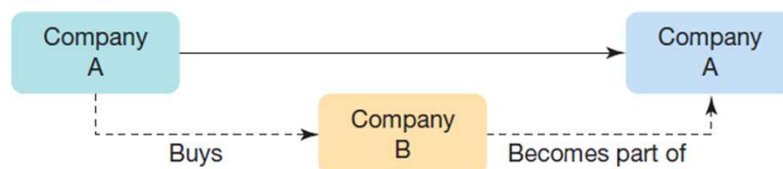
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## Options for Joining Forces

Merger



Acquisition

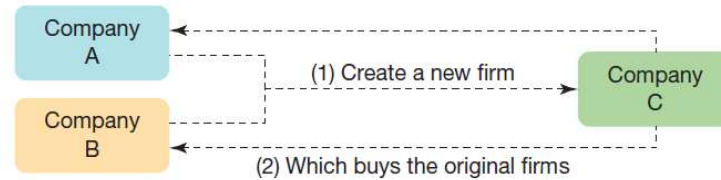


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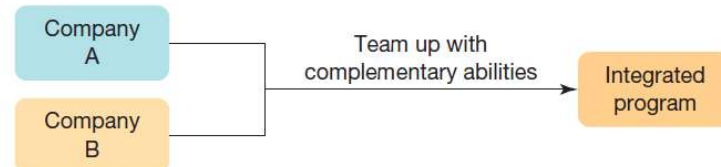
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## Options for Joining Forces (cont.)

### Consolidation



### Strategic alliance

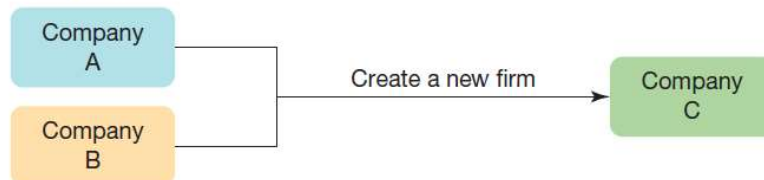


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27

## Options for Joining Forces (cont.)

### Joint venture



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28