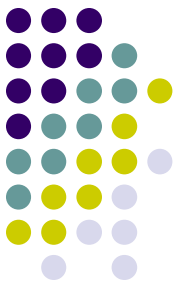
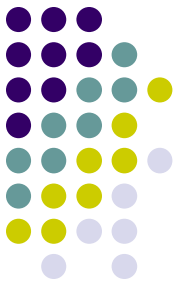


Factors to Consider when Choosing a Business Form



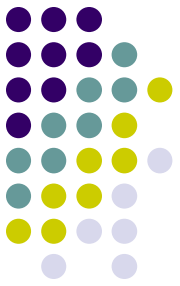
- **Ownership and Control**
 - (owners want to control how their businesses are operated)
- **Liability**
 - (shielding personal assets from liability for corporate debts)
- **Taxation**
 - (On which level will it be taxed?)
- **Expenses involved in formation**
 - (i.e. legal bills)
- **Capitalization**
 - (getting money for the business to operate and grow)
- **Liquidity**
 - (ability to resell shares of the company)

The Sole Proprietorship



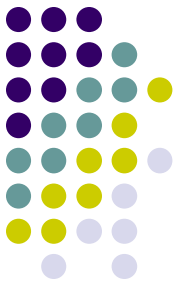
- Business owned by a single person
- No formation requirements at all... just open the doors and start operating
- Can contain employees; but one person has complete ownership and all decision making power
- **Taxation:**
 - All profits are considered personal income of the sole proprietor; there is no separate entity of the business itself
- **Liability:**
 - Proprietor is fully liable for all corporate debts

Sole Proprietorship



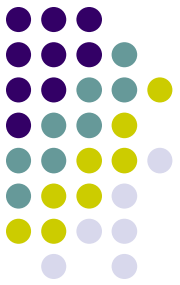
- **Advantages:**
 - Total control
 - Simplicity of Formation
- **Disadvantages**
 - Difficulty in raising capital
 - Unlimited Liability of owner for business debts
 - Very low liquidity in ownership of the business

General Partnership



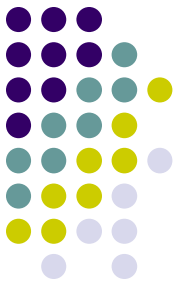
- One or more people have ownership stakes in the business
- Partnership is a contract; so each party to the partnership must have the capacity to form a binding contract
- A partnership is considered its own entity for some, limited purposes; but primarily, a partnership is the sum of the ownership parts
- Partnership agreements can be oral; but the best advice is to put it in writing
- Partnerships can be implied by a court if the partners held themselves out to the public as partners (partnership by “estoppel”)
- **Single taxation**
- similar to sole proprietorship in terms of liquidity and capitalization
- **VERY UNSTABLE;** As soon as any partner leaves the partnership, the whole partnership automatically dissolves

General Partnership – Default Rules



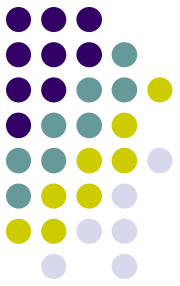
- Each partner has an equal ownership and control interest
- **Upon dissolution:**
 - First, all debts get paid off from business money
 - Second, partners' investments of capital get paid back
 - Left over money is split; with each partner getting his pro-rata share based on ownership interests

General Partnership - Example

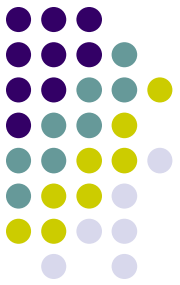


- **EXAMPLE:** Bart Lisa and Maggie have a partnership with no written partnership agreement that calls for anything specific to happen upon dissolution. Bart contributed \$500,000 to the partnership, Lisa contributed \$300,000 and Maggie contributed \$100,000.
 - If the partnership dissolves with \$1,500,000 in the bank and no debts, how much will each party receive?
 - If the partnership dissolves with no assets or debts, what will happen between the parties?
 - The partnership dissolves with no assets and \$1,200,000 in debts, who must pay what portion of the debt?

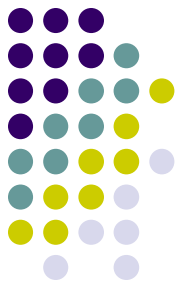
Answer to Partnership Dissolution Problem



- **Scenario A:**
- Each partner gets back his or her investment; then they split the remaining \$600,000 equally; so
 - Bart gets \$700,000 (\$500,000 originally invested plus his \$200,000 share)
 - Lisa Gets \$500,000 (\$300,000 originally invested plus his \$200,000 share)
 - Maggie gets \$300,000 (\$100,000 originally invested plus his \$200,000 share)

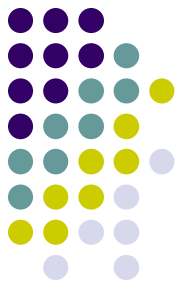


QUIZ TIME!



Answer to Partnership Dissolution Problem (cont.)

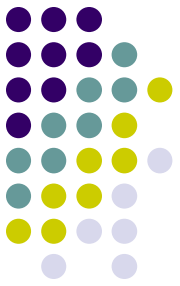
- **Scenario B:**
- Although there is no money in the partnership account, the original investments are “debts” of the partnership. Since there are \$900,000 in such “debts,” the partners must equally contribute toward that amount; So:
 - Bart receives a net of \$200,000 (\$500,000 he receives minus \$300,000 he must contribute)
 - Lisa breaks even (\$300,000 she receives minus \$300,000 she must contribute)
 - Maggie must pay \$200,000 (\$100,000 she receives minus \$300,000 she must contribute)



Answer to Partnership Dissolution Problem (cont.)

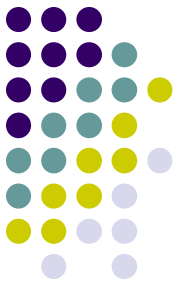
- **Scenario C:**
- The partnership debts total \$2,100,000 (the \$1,200,000 in debts plus \$900,000 in original contributions that must be paid back), which must be contributed equally. So:
 - Bart must pay \$200,000 (\$700,000 for his share of the \$2,100,000 debt minus the \$500,000 he receives as his initial contribution)
 - Lisa must pay \$400,000 (\$700,000 for her share of the \$2,100,000 debt minus the \$300,000 she receives as her initial contribution)
 - Maggie must pay \$600,000 (\$700,000 for her share of the \$2,100,000 debt minus the \$100,000 she receives as her initial contribution)

Limited Partnership



- Designed to keep the control, taxation and simplicity benefits of the partnership; while eliminating the problem of unlimited liability that plagues ordinary partnerships
- Requires a filing with the state (unlike the general partnership)
- **Split into 2 groups:**
 - General Partners: The “controllers”; they have the management function in the company and have unlimited liability; like other general partnerships
 - Limited Partners: The “investors”; they have no (or very limited) management functions and have limited liability (they cannot lose more than they invested)

Limited Partnership – Other Issues



- The Limited Partnership not dissolved automatically by the transferring of interest to a third party. Still, it's a pretty illiquid investment because it's hard to get a secondary market for shares in small partnerships.
- Taxation is same as with the general partnership and sole proprietorships (each partner is responsible for his or her taxes on his or her profits).
- Capitalization is easier than in a general partnership because people can invest without working at the business or assuming liability for partnership debts.