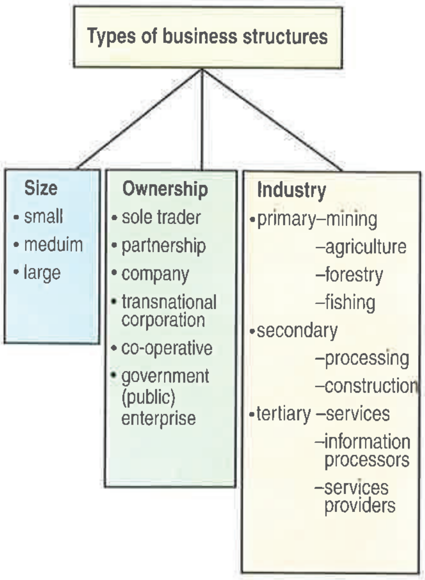
Types of business structures



[15.10] Types of business structures

proprietor
the owner or part owner of a business

unlimited liability
where the owner is responsible for all the debts of the business

[15.11] A hair salon, an example of a sole trader

Businesses are organisations that operate to satisfy people's wants. They may vary in size from small businesses (which may employ only a few people), to medium size businesses (employing hundreds of people), up to large businesses (which employ many thousands of people). Small businesses, of which there are many, are important to the Australian economy.

There are many different kinds of business structures in Australia today. We may classify businesses according to size, ownership and industry [15.10]. In fact, most businesses in Australia are small or medium-sized, employing fewer than a hundred people. It is estimated that there are over a million small businesses in Australia today.

Business can be classified, according to ownership, into sole traders, partnerships and limited liability companies. Companies may, in turn, be further subdivided into private and public companies.

The sole trader

A sole trader is the name given to a business that has only one owner. The owner or **proprietor** runs the business and, if successful, receives all of the profits from the business. The owner effectively is the business, and as such is liable for all of its debts if it does not succeed. The owner therefore has what is called **unlimited liability**. This means that if the business runs at a loss, it is the owner who suffers the loss. If the debts of the business are greater than the value of the assets (what the business owns) then the personal belongings of the owner may be seized and sold to pay the outstanding debts. The owner's luxury car, boat or holiday house may have to be sold to pay the debts of the business. The owner is allowed to keep personal items such as clothing, bedding and tools of trade.

A sole trader should also make provision for such things as sickness, accident and retirement, in case they are unable to work for long periods. Most sole traders therefore take out various forms of insurance.

The sole trader is the most common form of business organisation in Australia today. It is simple in structure and relatively small in size. To expand the business, the sole trader must obtain more finance, either from profits or by borrowing more money from the bank. This is often very difficult or expensive to do and so sole traders tend to remain relatively small in the size of their operations.

Examples of sole traders may be found in neighbourhood stores, small farms, tradespeople (electricians, builders), hair salons and restaurants.

Tony Corelli, builder: A case study

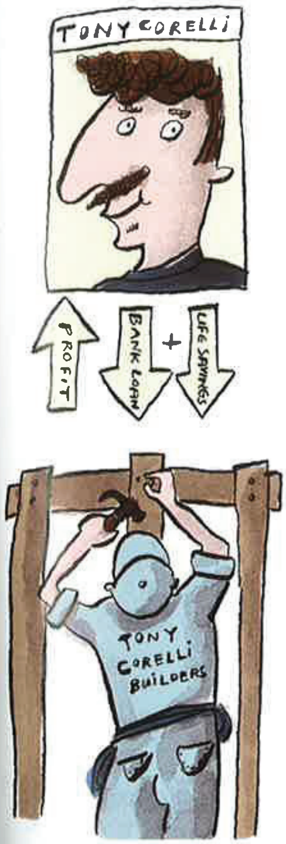
When Tony Corelli left school he worked for a building company, doing simple carpentry jobs. At night he attended carpentry classes at his local TAFE college and within a few years became a fully qualified carpenter. He worked as a carpenter for different companies, gaining experience all the time and earning good money.

After he had built up a sizeable bank account he decided to start up a business of his own. He approached his bank and obtained a loan. With his savings and loan money combined, he purchased a truck and the tools and equipment he would need to go out on his own.

Tony realised that he needed to advertise and so took out advertisements in the local paper. Before long he found he was attracting customers. He made sure he gave his customers good service and quality work. Satisfied customers then recommended him to their friends and gradually his business began to flourish.

Now Tony spends his day doing a variety of things. As a sole trader he takes phone calls from customers, visits them to quote on jobs, orders materials, does the banking and takes care of the financial records of the business. Many of the tasks, such as making phone calls and keeping business records, have to be done at night. As a sole trader Tony Corelli receives all the profits from the business. This means that he can keep the money he receives from customers, less his own expenses. Some of this money may be put back into the business to buy more tools and equipment or to buy a bigger truck.

Tony's business is now going so well that he is considering expanding further. He may decide to employ someone to answer the phone for him and do some paperwork while he is out on jobs. If he does this he must calculate that he can afford to pay this person wages and still make a profit for himself. Another possibility is to take on a partner (another builder) who would not only help him in his busy schedule but would add more finance to his expanding business.



[15.12] Tony Corelli, builder


>[15.13] Tony's truck on a building site

Partnerships

A partnership is a business that is owned by two or more people. By law a partnership can have up to twenty people but it is more usual to find partnerships that have between two and six partners. The partners share in the contribution of funds to the business, they generally share the workload as well as the profits (or losses). Although such sharing is generally equal, it need not be so. Partners who only contribute a small percentage of the funds—or capital—would probably expect only a small percentage of the profits. Some partners may contribute funds but are not able to share in the workload of the business. For example, a solicitor from a law partnership may become a politician but still wish to remain in the business (as a sleeping partner).

capital
the money initially invested in a business by the owner or owners

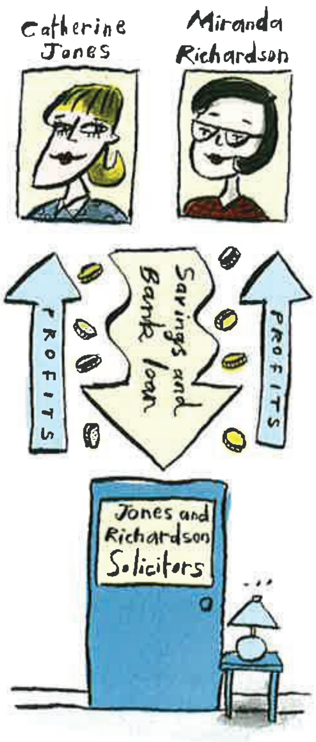
In order to have a partnership properly organised, it is advisable for the partners to make a partnership agreement. This agreement, drawn up on the advice of a solicitor or accountant, would set out such things as:

- the name and address of the business
- the type of business

- the names and addresses of each partner
- the duties and responsibilities of each partner
- the amount of capital each partner is to contribute
- how decisions affecting the business are to be made
- the way in which the profits are to be shared (generally this is in proportion to the amount of capital invested)
- what is to happen if one partner dies or wishes to leave the partnership.

[15.14] The advantages and disadvantages of partnerships

Advantages	Disadvantages
Partnership is able to attract more funds than a sole trader because several people are contributing	The owners are still liable for any debts (unlimited liability)
Easier for the business to borrow money	Each partner can be held personally liable for the debts of the business
The workload can be shared instead of one person trying to do everything	If one partner disappears and cannot be traced, the other partner or partners must pay the business debts
Sharing could lead to increased specialisation, with different people being responsible for different tasks	Possibility of disputes over the sharing of the workload and the profits
Allows each partner to become more efficient at the task they do best	
Greater efficiency is achieved by the partnership as a whole	



[15.15] Jones and Richardson Solicitors

In Australia, partnerships are most common in the professions (solicitors, doctors, dentists, accountants) and in the building trades (electricians, plumbers).

Jones and Richardson Solicitors: A case study

Miranda Richardson and Catherine Jones were good students at school. They both developed an interest in law back in Years 9 and 10 when they took Commerce as a subject. In senior school they studied Legal Studies and followed their interests further by studying law at university. When they had completed their degrees, each gained a position with a large law firm where they practised their profession for three years. When they felt they had gained enough experience the two friends decided to go into business together by forming a partnership. They drew up a partnership agreement in which they set out how they were going to organise their business.

Miranda and Catherine decided to be equal partners, contributing equal amounts of capital and sharing equally in the profits. They decided to specialise in terms of workload. Miranda was interested in conveyancing work (advising on the buying and selling of real estate) while Catherine specialised in family law (divorces, custody cases).

In their agreement they made allowance for the introduction of new partners into the business on the condition that the existing partners agreed.

Miranda Richardson and Catherine Jones felt that there were plenty of opportunities in the western suburbs of Sydney and so they rented premises in Penrith and hired a receptionist/secretary to make appointments for them. With their capital they also purchased some office furniture. It wasn't very long before the name Jones and Richardson Solicitors, became well-known in the Penrith area and the recommendations of satisfied clients assured them of a successful future.

2 Hold a class discussion on the advantages and disadvantages of going into business as a sole trader. Is a partnership safer?
3 Use the website for the Department of Employment, Workplace Relations and Small Business <www.dewrsb.gov.au> to find out what services the site provides. Make a list of them.
4 Working in groups, develop a partnership agreement for Jones and Richardson. Each group could compare their agreements to look for similarities and differences.

Companies

Companies are very different from sole traders and partnerships as a form of business organisation. A company is created by law and exists separately from its owners. It has 'perpetual succession', meaning that its existence does not cease if one of the members dies or becomes bankrupt. A company may sue or be sued and it may hold land in its own right.

The most important difference between a company and a sole trader or partnership is in the matter of liability. The owners of a company are called shareholders. Each shareholder contributes a certain sum of money to the company by buying shares. Thus each shareholder becomes a part-owner of the company. Under the Companies Act, shareholders have limited liability. This means that if the company is unable to pay its debts the liability of the shareholders is limited to the money they contributed when they bought their shares.

Shareholders, as part-owners, are entitled to a share in any profit made by the company. Naturally, the more shares a member owns the more profits they would be entitled to receive. When a company makes a profit it distributes some or all of it in the form of dividends.

Companies may be either private or public. A private company is referred to as a proprietary company and generally has the letters Pty Ltd after its name. The shares are offered privately to selected people and are not offered to the public for sale. A public company is one in which the shares are offered to the public for sale and these shares are traded openly on the stock exchange. Public companies, therefore, tend to be quite large with the advantage that they can attract large amounts of capital through the open sale of shares.

Did you know

A sole trader or partnership is dissolved by the death or bankruptcy of the trader or partner.

limited liability
where shareholders' obligations are limited to the amounts they have invested in a company

The stock exchange is covered fully in chapters 5 and 6.

Did you know

The letters Pty are short for proprietary and Ltd—short for limited—indicates that the company's shareholders have limited liability.

Incorporated associations

Another type of business structure, the incorporated association, is established and run much the same as a company except that the proceeds (or profits) do not go to shareholders but are used for the mutual benefit of members. Large licensed clubs are examples, such as the Parramatta Leagues Club Limited.

For more detailed information on clubs see chapter 13.

Learning about ...

1 What is the most important difference between a company and a sole trader or partnership?
2 What are the owners of a company called? What do they receive if the company makes a profit?