TOPIC: FORMS OF OWNERSHIP

Terminology

Capital is money provided by the owner(s) to set up the business.
Capital is used to buy assets such as land and buildings, vehicles, machinery and equipment.
Legal personality is the legal right of a person or business to own property, enter into contracts and sue or be sued.
If a business is a legal person, it is seen as a legal entity.
Continuity is the ability of the business to continue operating separately from the owner.
If a business has **no continuity** of existence, the business will stop existing if the owner retires or dies.
If a business **has continuity** of existence, the business will continue operating if there is a change of ownership.
A business that has a legal personality has continuity.
Liability is the owner's responsibility for the liabilities (debt) of the business.
If owners have **limited liability,** it means they cannot lose their personal belongings if there is not enough assets in the business to pay for the debts of the business.
If owners have **unlimited liability** it means they could lose their personal belongings if the business pays back all the debts.
Taxation – depending on the legal person of the business, either the owners or the business itself will pay tax on income or profits.
The owner of a sole trader and the partners of a partnership are responsible to pay tax on their personal income.
Close corporations and companies are seen as legal entities therefore these businesses are responsible to pay income tax on profits made.
Tax is paid at a fixed percentage of 28% on profits and a secondary tax of 10% on profits paid out to members or shareholders.

Description of the forms of ownership

Sole trader (characteristics)

Number of owners	1
What owners are called	Owner
Amount of capital	Contributes own capital Can borrow from bank
Name requirements	No restriction to the name, e.g. Thandi's Bakery
Legal status	Not a separate legal entity
Liability for debt of the business	Unlimited liability. Creditors can take the personal assets if the business is in debt.
Formation of the business	Very easy form, no registration required except perhaps a trading license from the local authority.
Division of profits	All the profits belong to the owner
Documentation	No documents required

- **Impact of a sole trader (Advantages and/or disadvantages)**

Advantages	Disadvantages
Owner makes all decisions.	Unlimited liability which means the owner is responsible for all debts incurred.
Requires little capital to start.	Cash flow is often a problem.
All profits belong to the owner	Growth of business can be restricted due to lack of capital.
Simple management structure.	Not a legal entity and no continuity
Can easily adapt to the needs of the customer.	Difficult to attract highly skilled and knowledgeable employees.
No legal process and requirements.	The owner is responsible for providing all the capital needed.
The assets of the business belong to the owner.	If the owner does not have enough knowledge or experience the business may fail.
There is personal encouragement and personal contact between the owner and customers.	

Partnership (characteristics)

Number of owners	Minimum of 2 but there is no limitation on the number of partners
What owners are called	Partner
Amount of capital	Partners contribute capital in the form of cash, assets or skills.
Name requirements	No restriction to the name, e.g. Thandi & Mpho's Bakery
Legal status	Not a separate legal entity
Liability for debt of the business	Unlimited liability. Partners are jointly and severally liable for all debt
Formation of the business	Only needs a trading license from the local authority.
Division of profits	Partners share their profits according to their Partnership agreement
Documentation	An oral or written partnership agreement

- **Impact of a partnership (Advantages and/or disadvantages)**

Advantages	Disadvantages
The partners are able to put their knowledge and skills together to collectively make the best decisions.	A partnership has unlimited liability
The workload and responsibility is shared between partners.	Each business partner is legally responsible for the joint liability of the partnership.
Partners are able to share resources.	Different personalities and options of partners can lead to conflict.
Partners are only required to pay tax in their personal and individual capacity.	Partners might not all contribute equally.

The partners have a personal interest in the business.	Loss in profits and stability of the business can occur if a partner resigns/ dies/loses interest in the business or is declared bankrupt.
Can bring in extra partners at any time.	There can be lack of capital and cash flow.
Attract prospective employees with the option or incentives of becoming a partner.	

Close Corporation (CC) (characteristics)

Number of owners	1 – 10
What owners are called	Members
Amount of capital	Limited to the 1-10 members contribution.
Name requirements	Name must be registered and ends with CC The Reading Room CC
Legal status	A separate legal entity
Liability for debt of the business	Limited liability. Only responsible for the capital contributed.
Formation of the business	No new CCs can be registered in South Africa after 1 May 2011, but CCs can convert through the CIPC to a private company.
Division of profits	Profits shared in proportion to the member interest in the CC.
Documentation	Founding statement was required at the time of registration

- **Impact of a Close Corporation (Advantages and/or disadvantages)**

Advantages	Disadvantages
There are few legal requirements e.g. auditing of financial statements/regular annual general meetings.	Limited growth and expansion since a CC cannot have more than ten members.
A CC is a legal entity and has continuity of existence.	A member of a CC can be held personally liable for the losses of CC if the member acts is incompetent.
Can be converted to a private company and members may become shareholders.	Audited financial statements may be required when applying for a loan.
Members have limited liability	A CC is taxed as if it were a company, which may be higher than personal tax rates.
Owners' interest in the CC does not need to be in proportion to their capital contribution.	Difficult for members to leave the CC as all members must agree to dispose of a member's interest.
CC may be exempted by CIPC from auditing its financial statements.	A CC is taxed on its income and Standard Tax of Company (STC) based on member's dividends.

Private company (Pty) Ltd (characteristics)

Number of owners	1 or more shareholder
What owners are called	Shareholders
Amount of capital	Shares may not be offered to the public and the right to transfer shares is restricted.
Name requirements	The name of the business ends with (Pty) Ltd
Legal status	A separate legal entity
Liability for debt of the business	Limited liability
Formation of the business	All companies must register with the Companies and Intellectual Property Commission (CIPC)
Division of profits	Profits shared in the form of dividends in proportion to the shares held.
Documentation	Memorandum of Incorporation (MOI)

- **Impact of a Private Company (Advantages and/or disadvantages)**

Advantages	Disadvantages
More opportunities to pay less taxation	Requires a lot of capital
Good long-term growth opportunities	The more shareholders, the less profits
Own legal identity and shareholders have limited liability.	More taxation requirements
Board of directors with expertise can be appointed to take decisions.	Directors do not have a personal interest
Not required to file annual financial statements with the CIPC.	Annual financial statements must be reviewed by a qualified person, which is an extra expense to the company.
It is a legal person and can sign contracts in its own name.	Difficult and expensive to establish as the company is subjected to many legal requirements
The new Act forces personal liability on directors who knowingly participated in carrying out business in a reckless or fraudulent manner.	Pays tax on the profits of the business and on declared dividends.
Financial statements are private and not available to the general public.	Must prepare annual financial statements.
A company has continuity of existence	
It is possible to sell a private company as it is a legal entity in its own right.	

Public company (Ltd) (characteristics)

Number of owners	1 or more shareholder
What owners are called	Shareholders
Amount of capital	Shares are sold to the public through the JSE.
Name requirements	The name of the business ends with Ltd
Legal status	A separate legal entity
Liability for debt of the business	Limited liability
Formation of the business	All companies must register with the Companies and Intellectual Property Commission (CIPC)
Division of profits	Profits shared in the form of dividends in proportion to the shares held.
Documentation	Memorandum of Incorporation (MOI)

- **Impact of a Public Company (Advantages and/or disadvantages)**

Advantages	Disadvantages
The business has its own legal identity	Must disclose all financial information
Easy to raise funds for growth through the sale of shares.	Large amount of funds are spent on financial audits.
Shareholder is only liable for the amount which is invested.	Stocks have to be traded publicly.
Can appoint a knowledgeable board of directors.	A full report must be submitted to the major shareholders each year.
Buy and sell shares freely.	Difficult and expensive to establish as the company is subjected to many legal requirements.
Shareholders can sell or transfer their shares freely.	The more shareholders, the less profit.
The public has access to the information and this could motivate them to buy shares from a company.	Shareholders may be allowed little or no input into the affairs of the company.
Additional shares can be raised by issuing more shares or debentures	Due to legislation, decisions take longer and there may be disagreements.

Differences between the private and public company

Private Company	Public Company
May not offer shares to the general public.	Trades its shares publicly on the Johannesburg Securities Exchange.
Shares are not freely transferable	Shares are freely transferable.
Minimum of one director.	Minimum of three directors.
Name must end with (Pty) Ltd.	Name must end with Ltd.
Annual financial statements need not be audited and published.	Annual financial statements need to be audited and published.
Does not need to publish a prospectus as it cannot trade its shares publicly.	Have to register and publish a prospectus with the Companies and Intellectual Property Commission (CIPC).

TOPIC: FORMS OF OWNERSHIP – ACTIVITY

1. Match the description in Column B with the correct word in Column A. Write **ONLY** the correct letter (A – K) next to the numbers (1.1 – 1.9) on the folio paper provided, e.g. 1.10 L.

Column A	Column B
1.1. Sole trader	A. A legal business entity that was registered by submitting a founding statement.
1.2. Partnership	B. It is very easy to start and business decisions can be made quickly.
1.3. Close corporation	C. Providing job opportunities for their workers to learn new skills so that they will always have a job in the business.
1.4. Private company	D. A business that can only be owned by one person.
1.5. Public company	E. A business that is not registered as a legal person and that has an unlimited number of owners.
1.6. A disadvantage of a partnership	F. A legal business entity that can have an unlimited number of owners, whose shares can be bought on the JSE.
1.7. An advantage of a close corporation and a company.	G. A legal business entity that can have an unlimited number of owners, whose shares can only be sold if the other shareholders agree.
1.8. A disadvantage of a company	H. There is an effort to limit the amount of resources used.
1.9. An advantage of a sole trader	I. There are many legal formalities that have to be followed to start the business.
	J. It has limited liability.
	K. It has unlimited liability. (9)

2. Use the word bank below and then choose the most suitable name for the form of ownership mentioned in question 4.4.1 – 4.4.5, e.g. 4.4.6 cooperatives.

Patel & sons; Tau Food Group (Pty) Ltd; ACSA (SOC) LTD.; The Reading Room CC; The Mining Experts Ltd; The Legal Specialists Inc; Thandi's Hair Salon

2.1 Close Corporation
2.2 Sole trader
2.3 Private company
2.4 Partnership
2.5 Public company (5)

3. Describe **THREE** advantages and **THREE** disadvantages of a
   3.1 sole trader (6)
   3.2 partnership (6)
   3.3 Private company (6)
   3.4 Public company (6)
4. Name a form of ownership with limited liability. (1)
5. Differentiate between a private company and a public company. (8)