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Formation of business entities Business entity laws govern the formation, running, control and disclosure of each business entity. Sole proprietorships and partnerships do not require complex requirements in their formation and dissolution but the owners bears the liabilities of the business personally. Corporations and Limited Liability Companies are separate legal entities. Franchise business is governed by Federal Trade Commission Rules on disclosure and the applicable State statutes.

Formation of business entities

Introduction

There are numerous laws that govern the formation, running and control of business entities. Sole proprietorship is the first and the simplest form of business entity (Emerson, 2009). Sole proprietorship is a business formed and controlled by the same person whereby the owner shares all profits and risks in the business (Balotti, 2011). A sole proprietor bears all the liabilities of the business including all debts, violations and losses associated with the business. From my professional experience, some of the advantages of a sole proprietorship include the ease of formation since only a business name and business license is needed to start the business (Emerson, 2009). The sole proprietor enjoys all the profits, decision making and control of the business. A small amount of capital is needed to form the business and tax benefits arise since tax returns are not filled as a separate business but as personal income of the business owner (Emerson, 2009).

However, some disadvantages of a sole proprietorship business include the difficulties in securing expansion capital in the capital markets, the lack of continuity after the death or incapacitation of the sole proprietor and the direct responsibility for all debts, losses and business violations of the sole proprietorship business (Balotti, 2011).

The second common form of business entity is the partnership. Some types of the partnership include the general partnership and limited partnership. General partnership business is created under common law where two or more people form a business with the sole objective of making a profit. It is created by partnership agreement that outlines the duties and method of sharing profits and losses amongst the partners (Emerson, 2009). Without such agreement, the profits and losses are shared equally amongst the partners. In my own experience, partnership has certain disadvantages since each partner is jointly liable for the wrong actions of the other partners and the business can terminate after the death, bankruptcy or on agreement of the partners (Emerson, 2009).

The Uniform Liability Partnership Act of 2001 permitted the establishment of limited partnerships whereby the debts of the limited partner will be the sole responsibility of the partnership business (Emerson, 2009). Limited partnerships should disclose the status of the limited partner while dealing with third parties and file documents with the relevant registration authorities in each State (Humphreys, 1998). Generally, the limited partner has low input in control and decision making process and mainly provides capital for the business. From professional experience, limited partnerships are ideal for special projects but the general partners will be jointly liable for the liabilities of the limited partner (Balotti, 2011).

The fourth form of business entity is the Corporation. This is the common business organization in the United States of America whereby the business exists as separate legal entity and shareholders are shielded from personal liability of the debts and losses of the business. There are numerous laws that govern the formation of Corporations in the US but the main two are the Model Business Corporation Act and Delaware General Corporation Law (DGCL). Publicly traded corporations that are listed in the capital markets are expected to comply with Sarbanes-Oxley Act of 2002 on financial reporting and Securities Exchange Act of 1934 which govern the trading and issuance of shares on the capital markets (Balotti, 2011). A Corporation is thus a legal entity that is incorporated according to the particular corporate law and which can sue or be sued in its own right or enter in to contracts with third parties while conducting the business of the corporation (Humphreys, 1998). The duties and rights of shareholders and powers of directors are outlined in the corporate charter and memorandum of association (Balotti, 2011).

Limited liability Company (LLC) is a form of unincorporated business entity whereby the relationships of the members is governed by agreements. This form of business entity is governed by State statutes and members have a limited liability. Members can participate in the management and it is treated just like a partnership in taxation purposes (Balotti, 2011).

Franchise is the last form of business entity whereby one business buys the rights to utilize another successful business model. The franchisor licenses some trademarks to the franchisee in exchange of recurring franchise fee (Balotti, 2011). From experience, some States accept franchises while others limit the establishment of this business entity through business opportunity laws. Federal Trade Commission Rule guides the establishment of franchise business through disclosures and prohibitions on franchises. The franchisor must issue a disclosure statement fourteen days prior to sell of the franchise. From professional experience, a franchise will allow for rapid business expansion but the main disadvantage is the loss of business control. Some states like Illinois, California, Michigan and New York states have different statutes that govern the registration and renewal of franchises (Balotti, 2011).

Conclusion

Each form of business entity is governed by different laws. Sole proprietorship is the easiest form of business organization but the owner bears all the losses of the business. Model Business Corporation Act guides the formation of Corporations while Federal Trade Commission Rule provides the guidelines of franchising.

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