GAUTENG PROVINCE
EDUCATION
REPUBLIC OF SOUTH AFRICA

BUSINESS STUDIES
GRADE 11
TERM ONE
CHAPTER FIVE

BENEFITS OF THE COMPANY OVER OTHER FORMS OF OWNERSHIP

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This chapter consists of 16 Pages

CONTENT DETAILS FOR TEACHING, LEARNING AND ASSESSMENT PURPOSES

BENFITS OF A COMPANY OVER OTHR FORMS OF OWNERSHIP

Learners must be able to:

- Discuss/Explain/Describe the characteristics, advantages and disadvantages of the forms of ownership. (Recap)
- Distinguish/Differentiate/Tabulate the differences between forms of ownership.
- Discuss/Explain the benefits of establishing a company versus other forms of ownership e.g.:
  - Legal status and liability.
  - Profit sharing
  - Ownership and management
  - Capital and cash flow
  - Life span and continuity
  - Taxation
- Discuss/Explain the challenges of establishing a company versus other forms according to the above mentioned benefits.
- Explain/Describe/Discuss the procedure for the formation of companies.
- Discuss/Explain the legal requirements of the name of the company, e.g.:
  - A company is not allowed to use a misleading name,
  - A name reservation is valid for six months, etc.
- Define the following concepts:
  - Memorandum of incorporation
  - Notice of incorporation
  - Prospectus, i.e. initial & secondary offer
- Outline the aspects that must be included in the prospectus.

TERMS AND DEFINITIONS

TERM	DEFINITION
Form of ownership	The legal position of the business and the way it is owned.
Continuity	Continue to exist even if a change of ownership takes place, e.g. a member or shareholder dies or retires.
Securities	Shares and bonds issued by a company.
Limited liability	Loses are limited to the amount that the owner invested in the business.
Unlimited liability	The owner's personal assets may be seized to pay for the debts of the business.
Memorandum of Incorporation (MOI)	The document that sets out the rights, responsibilities and duties of shareholders and directors.(serves as a constitution of a company).
Sole Trader /Sole proprietor	A business is owned and controlled by one person who takes all the decisions, responsibility and profits from the business they run.
Partnership	An agreement between two or more parties that have agreed to finance and work together in the pursuit of common business goals.
Co-operative society	Autonomous association of persons united voluntarily to meet their common economic/ social needs/aspirations through a jointly owned and democratically controlled enterprise.
Company	A company is a legal person who has capacity and powers to act on its own.
Public company	A public company is a voluntary association of ONE or more persons, governed by the company Act 71 of 2008, incorporated in terms of the Memorandum of Incorporation.
Private company	A private company is a voluntary association of 1 or more persons.
Personal liability company	A personal liability company is a voluntary association of 1 or more person.
State-Owned company	A state-owned company (SOC) is a legal entity that is created by the government in order to participate in commercial activities on its behalf.
Partnership Article	A document that contains exhaustive provisions with regards to the matters concerning the business and the partners.
Prospectus	Prospectus is a document inviting the public to buy securities/shares.
Annual General Meeting (AGM)	A meeting held once a year where the shareholders receive a report stating how well the company has done.
Directors	People elected to the board of a company by the shareholders to represent the shareholders' interests.

1 CHARACTERISTICS, ADVANTAGES AND DISADVANTAGES OF THE FORMS OF OWNERSHIP. (RECAP)

1. SOLE TRADE /SOLE PROPRIETOR

Definition

A sole trader is a business that is owned and managed by one person.

Characteristics of a sole trader

- One person can form a sole trader and is easy to start.
- It is inexpensive to start and the owner does not have to pay tax.
- There are no legal and administrative formalities in the formation of a sole trader.
- The profit of the business is belongs to the owner as there is no distinction between the owner and the business.
- A sole proprietor is not a legal entity and agreements are entered into by the owner in his\her personal capacity.
- Business has unlimited liability and the private possessions of the owner can be used to pay the debts of the business

2 Advantages and disadvantages of a sole trader

ADVANTAGES	DISADVANTAGES
-Owner makes all decisions.	-Unlimited liability which means the owner is responsible for all debts incurred by the business
-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 client/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/experience the business may fail.
-There is personal encouragement and personal contact between the owner and customers.	

2 PARTNERSHIP

2.1 Definition

- A partnership has two or more partners who own the business.
- These owners share the responsibility of the business and they share the financial and management decision of the business.

2.2 Characteristics of a partnership

- An agreement between two or more people who combine labour, capital and resources towards a common goal.
- Partners combine capital and may also borrow capital from financial institutions.
- No legal requirements regarding the name of the business.
- Partners have unlimited liability and are jointly and severally liable for the debts of the business.
- Profit is shared according to the partnership agreement.
- Partnership does not pay tax partners pay personal income tax.
- Auditing of financial statements is optional.
- Partners share responsibilities and they are all involved in decision making.
- No legal formalities to start, only a written partnership agreement is required.
- The partnership does not pay income tax, only the partners in their personal capacities.
- Diversity, specialisation and different skills of the partners can be used.
- Partnership has no legal personality and therefore has no continuity.
- Partners share responsibilities and they are all involved in decision making.

2.3 Advantages and disadvantages of partnership

ADVANTAGES	DISADVANTAGES
-The partners able to put their knowledge and skills together to collectively make the best decisions.	-A partnership has unlimited liability so all the partners are liable for the debts if the business becomes insolvent.
-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 it disagreements.
-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.	
-Partnerships are relatively easy to establish.	
-Partners contribute new skills and ideas into a business	
-Partners share responsibilities for decision making and managing the business	
-Partners share any profits and are therefore motivated to work hard.	
-Raising additional capital to finance further business expansion is easy as there is no limit on the number of partners.	
-Partners are taxed in their own capacities, which could lead to lower taxation.	

3 CLOSE CORPORATION

3.1 Characteristics of a Close Corporation

- Can have a minimum of one and maximum of ten members who share a common goal.
- The word ‘close’ means that all members are involve and participate in its management.
- Each member makes a contribution of some/assets/services towards the corporation.
- The name must ends with the suffix CC.
- Members have unlimited liability except where the CC has had more ten members for six months or longer.
- A CC has its own legal personality and therefore has unlimited continuity.
- Auditing of books is optional as members only need an accounting officer to check financial records.
- Transfer of a member’s interest must be approved by all other members.
- Profits are shared in proportion to the member’s interest in the CC.

3.2 Advantages and disadvantages of a Close Cooperation

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/ Double taxation.

4 Private Company

4.1 Definition

It can be a small or large company and has one or more directors.

4.2 Characteristics of a private company

- Requires one or more directors and one or more shareholders.
- It needs a minimum of one shareholder and there is no limit on the number of shareholders that a private company may have.

- Register with the registrar of companies by drawing up Memorandum of Incorporation.
- The company name ends with letters (PTY) Ltd.
- A private company is not allowed to sell shares to the public.
- Investors put capital in to earn profit from shares.
- The company has a legal personality as well as unlimited continuity.
- The auditing of financial statements is optional.
- Profits are shared in the form of dividends in proportion to the share held.
- Shareholders have a limited liability and will not lose their initial capital invested if the business goes bankrupt.
- Shareholders have limited liability and a separate legal entity.
- Raises capital by issuing shares to its shareholders.
- Profits are shared in the form of dividends in proportion to the number of shares held.

4.3 Advantages and disadvantages of a private company

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 no direct legal implications/ limited liability.	-More taxation requirements
-Board of directors with expertise /experience can be appointed to take decisions	-Directors do not have a personal interest
-Not required to file annual financial statements with the commission.	-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/fraudulent manner.	-Pays tax on the profits of the business and on declared dividends/Subject to double taxation.
-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.	
-It can easy raise capital by issuing shares to its members.	

5 PERSONAL LIABILITY COMPANY

5.1 Definition

- Very similar to a private company, the difference is that the directors of a Personal Liability company are jointly and severally liable for all the debts and liabilities of the company. This means that the directors have unlimited liability.
- The name of the personal liability company ends in INC and the name of the private company ends in (PTY) Ltd.

5.2 Characteristics of a personal liability company

- The company name must end with letters INC
- Directors have unlimited liability and they are jointly liable for the debts of the business even if they are long out of office.
- The memorandum of Incorporation should state that it is a personal liability company.
- They must at least have one director on their board of directors.

NOTE: Other characteristics of a personal liability company are the same as the private company except the above mentioned two characteristics.

5.3 Advantages and/or disadvantages

NOTE: The advantages of a personal liability company are the same as the private company.

The disadvantages are also the same as the private company except the directors of the personal liability company have unlimited liability

6 PUBLIC COMPANY

6.1 Definition

- A public company is a company that is registered to offer its stock and shares to the general public. This is mostly done through the Johannesburg Securities/Stock Exchange (JSE).
- The public company is designed for a large –scale operation that require large capital investments.

6.2 Characteristics of a public company

- A minimum of one person is required to start a public company.
- Requires three or more directors and three or more shareholders.
- Register with the Registrar of Companies by drawing up Memorandum of Incorporation.
- The company name ends with letters Ltd.
- Has legal personality and therefore has unlimited continuity
- Raises capital by issuing shares to the public and borrowing capital by issuing a debenture.
- A prospectus is issued to the public to raise capital.
- Shareholders have a limited liability
- The new Act forces personal liability on directors who knowingly participated in carrying out business in a reckless/fraudulent manner.
- The company has a legal personality as well as unlimited continuity.

- A public company is required to hold an AGM (Annual General Meeting).
- Auditing of financial statements us compulsory and audited statements are available to shareholders and the public.
- Profits are shared in the form of dividends in proportion to the share held.

6.3 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/Shareholders have limited liability.	-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/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.
-Strict regulatory requirements protect shareholders.	-Financial affairs must be known to publicly, this information could be used to competitors' advantage.

7 State owned company

7.1 Definition

- A state owned company has the government as its major shareholder and falls under the department of Public Enterprise.
- These businesses take on the role of commercial enterprise on behalf of the government.

7.2 Characteristics of a State Owned Company

- Requires three or more directors and one or more shareholders.
- Register with the Registrar of Companies by drawing up Memorandum of Incorporation.
- It is owned by the government and operated for profit.
- SOC is listed as a public company.
- The name ends with letters SOC.
- State –owned companies support private businesses by providing infrastructure such as communication service /Post office and supply of electricity/Eskom.

7.3 Advantages and disadvantages

Advantages	Disadvantages
-Profits may be used to finance other state departments	-May result to poor management as government is not always as efficient as the private sector.
-Offer essential services which may not be offered by the private sector	-Inefficiency due to the size of the business
-Prices are kept reasonable/Create sound competition with the private sector to make services affordable to more citizens.	-Often rely on government subsidies
-Wasteful duplication of services is eliminated	-A lack of incentive for employees to perform if there is no absence of other motivator such as productivity bonuses.
-Planning can be coordinated through central control.	-Government can lose money through the business.
-Generates income to finance social programmes.	-A lack of incentive for employees to perform if there is no share in the profit.
-Jobs are created for all skills levels.	-Losses must be met by the tax payer.
	-Shares are not freely tradable making it difficult to raise capital.
	-SOC must follow strict regulations for operations to raise capital.
	-Financial statements must be audited

8 Differences between the private and public company

PRIVATE COMPANY	PUBLIC COMPANY
- May no 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 Proprietary Limited/(Pty) Ltd.	- Name must end with Limited/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.
- The company is not required to raise the minimum subscription/ issue minimum shares.	- Must raise a minimum subscription prior to commencement of the company.

9 Differences between the private and a personal liability company

PRIVATE COMPANY	STATE OWNED COMPANY
The name ends with (PTY) Ltd	The name ends with INC
The directors are not personally liable for the debts of the business.	The directors are personally liable for the debts of the business.

10 Cooperatives

10.1 Definition

- A cooperative is a traditional way of a group of interested parties getting together and sharing resources/infrastructures and costs to achieve a better outcome.

10.2 Characteristics of cooperatives

- Minimum of five members is required to start a cooperative.
- Register with the Registrar of Companies
- Legal entity and can own land and open bank accounts.
- Members own and run the business together and share equally in its profits.
- Decisions are taken democratically
- They are motivated by service rather than profit
- Must register with the Registrar of Cooperatives Societies
- The word 'Cooperative Limited' must appear at the end of its name.
- They are managed by a minimum of three directors.
- The objective of a co-operative is to create mutual benefit for the members.

10.3 Advantages and/or disadvantages of cooperatives

ADVANTAGES	DISADVANTAGES
-Access to resources and funding	-Decisions are often difficult to reach and time consuming.
-Decision making is by a group	-Difficult to grow a co-operative.
-Each member has an equal share in the business.	-Very few promotion positions for staff.
-A co-operative can appoint its own management.	-It can be difficult to get a loan because their main objective is not always to make a profit.
-Members have limited liability	-The success of cooperatives depends on the support of the members.
-The decisions are democratic and fair	-Shares are not freely transferable
-Members are motivated because they are working for themselves	-All members have one vote regardless of the number of shares held.
-Can gain extra capital by asking its members to buy shares.	
-Co-operatives have continuity of existence	
-Resources of many people are pooled together to achieve common objectives	
Profits are shared equally amongst members.	

11 Benefits of establishing a company versus other forms of ownership

11.1 Legal status and liability

- A company has its own legal status, trading name and owns its assets.
- Shareholders' private assets are protected as they have limited liability.
- The shareholders have no direct legal responsibility.
- Companies have their own names and these are protected.

11.2 Profit sharing

- Shareholders share in the profits of the company through dividends

11.2 Ownership and management

- Shareholders are able to buy and sell shares freely in a public company.
- The company is managed by qualified and competent board of directors
- A company is less likely to use consultants as it has a larger pool of skills and expertise
- Directors are more likely to take risks and allow growth opportunities for the business.

11.3 Capital and cash flow

- A company may has more investor's to fund the setting up of the business.
- Companies have a better cash flow than sole traders.
- A company is not limited to the individual contribution of the members' capital.
- The long term growth opportunities for companies are really good as there are always possibilities of getting in more investors.
- Directors do not have to take out personal loans to grow the business

11.4 Life span and continuity

- A company has continuity of existence.
- Company shares can be transferred/bought/sold.
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11.5 Taxation

- Companies have tax benefits other enterprises do not have
- They may obtain tax rebates if they are involved is social responsibility projects.

12 Challenges of establishing a company versus other forms of ownership

- Directors may not have a personal interest in the business and this could prevent the business from gaining maximum growth and profits.
- Directors who do not have a personal interest in the business may not attract investors.
- There may be conflict between the owners of the company and management in control.
- The more shares there are the less profit per share.
- A company is required to submit a full report to all stakeholders each financial year.
- The limited liability aspect of the company generates more paper work in the registration process.
- The owners of the company have more liability.
- When directors change there could be a lack of continuity in management.

- Companies have more taxation requirements and other taxes are high.
- They are required to disclose all financial information which could provide their competitors with an unfair advantage.
- Politics can get in the way and managers are appointed for the wrong reasons.
- State owned companies often deliver non-profitable services that lead to government losing money through the business.
- A company can stop existing if deregistered by the Registrar of Companies.
- A large amount of money of funds is spent on financial audits and accounting fees due to government regulations.

13 Procedure for the formation of companies

- Determine the people establishing the company
- Reserve a company name with the Registrar of Companies
- Prepare a memorandum of incorporation
- File a notice of incorporation
- Obtain a unique registration number
- All companies must be registered with the Registrar of Companies.
- Open a bank account and register for taxation.
- Draw up a prospectus for potential investors.

14 Legal requirements of the name of the company

- The name of a company must be original and must not be misleading.
- A company's name must appear on all company documents, e.g. on letterheads.
- Reserving a name for a company is the first step to register a company , but it is not compulsory.
- Names can be reserved for a period of 6 months by the CIPC.
- The name must not be similar/same as any other company unless it is part of the group.
- The name must not imply/suggest/mislead a person to believe that the company is part of another person/business/the state.
- The name must not be offensive/promote violence/hatred and cause any harm.
- The name must not be shortened and translated.
- The name of a company must indicate the type of company as follows: The name of a company must end with.

15 Memorandum of incorporation/MOI

15.1 Meaning of memorandum of incorporation/MOI

- MOI serves as the constitution of a company.
- Companies are governed according to the rules stated in the MOI.
- Each company must provide a copy of its MOI to the Companies and Intellectual Property Commission (CIPC).
- MOI describes the relationship between the business and its stakeholders.
- MOI describes the rights, responsibilities and duties of the shareholders and directors.
- Provides details about incorporation, the number of directors and the share capital.
- Includes information about a company's name/registration office and records.

15.2 Aspects that must be included in the memorandum of incorporation

- Incorporators
- Nature of the company
- Securities of the company
- Shareholders and meetings
- Directors and officers
- Name of the company
- Main objectives of the company
- Number of shares each incorporator will purchase
- Amount of share capital registered
- Rules and regulations of the company
- Name of the auditor

16 Notice of incorporation

- The notice must be lodged together with the Standard Form of Memorandum of Incorporation and it contains the following information
  - Type of company
  - Financial year-end
  - Numbers of directors
  - Incorporation date
  - Registered address
  - Company name

17 Prospectus

17.1 Meaning of a prospectus

- A prospectus is a written invitation to the public to buy the securities offered by a public company.
- It is a formal legal document giving details about investment offerings to the public.
- A prospectus can only be issued by a company and it must be within three months after the date of its registration.
- It gives information about the business.

17.2 Meaning of the Initial order offer/IPO

- This is when the company issues shares to the public for the first time.
- The company must produce a prospectus before undertaking the initial offering.
- Most companies undertake an IPO with the assistance of an investment banking firm acting in the capacity of an underwriter.

17.3 Meaning of the secondary offering

- A secondary offering is an offering of securities by a shareholder of the company as opposed to the company itself, which is a primary offering
- A secondary offering is the sale of new or closely held shares by a company that has already made an initial public offering (IPO)

17.4 Aspects that must be included in the prospectus

- Company overview, including the vision, mission and goals of a business
- Product or service portfolio
- Market analysis and strategy
- Management team
- The risk and potential of the business
- Available financial and share information
- Company's assets and liabilities
- Financial position
- Profits and losses
- Cash flow
- Prospects for growth
- Pre-incorporation contracts that have been signed
- Date of registration of the prospectus
- The minimum subscription