Business Formation

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# Strengths and Weaknesses of Partnership Business

A partnership is a form of business organization wherein two or more than two people enter a legal contract to form business operations. The partners invest their own funds and skills in a business and share the profit earned by the enterprise. The two forms of partnership business are a general partnership and limited partnership, each has its own merits and demerits. In the case of general partnership, no business taxes are to be paid, and hence there is no double taxation. The partnership business is easy to establish and the liability is also shared by more than a single owner. Partnership pools the talent and money and also results in the good management of business operations. A limited partnership allows one of the partners to keep their liability limited and save themselves from the vulnerability of any potential lawsuit.

They also get the advantage of sharing profit and loss without participating in business operations. This form of business entity has some shortcomings as well, for instance, in the case of a general partnership, partners are mutually and individually liable for the business obligations. Partners cannot take any decision without the consent of other partners and the death of any of the partner can also lead to the dissolution of the business. Overall, the partnership business has always the risk of conflicts arising from differences in work and funds contributed to the business.

# Benefits and Shortcomings of a Corporation

A corporation is a legal entity that separates the business from its owners. The corporation is taxed, generates profit and can be sued by some external parties (Vermeulen, 2003). Generally, corporations raise funds by issuing shares and bonds to the general public and people who provide finance to the company are named as the owners of shareholders of the company. It is treated as a separate entity from its owners and people who manage its operations. One of the major benefit that a corporation offers is limited liability of its owners. The only loss owners may need to face in case of business failure is the loss of money invested in the company and they are not held personally liable for any obligations of the company. The corporation can raise a considerable amount of money to run business operations. In addition, there is no limitation to the life of this business entity.

Some of the detriments of starting a business as a corporation are double taxation, once on the income of the company and secondly on the income of shareholders. It is also expensive to create this business entity in comparison with the partnership business. In addition, when the corporation is started it comes with excessive paperwork. Though there is one exception to this scenario that is S corporation wherein the profits and loss of the company are passed to the shareholders. The management of the corporation is held by a separate team that can have different interests than the owners of the corporation.

# Choosing the Best Option

In the given scenario, three personal trainers are looking forward to commencing a health club, and the dilemma is to choose the right form of business organizations to commence the operations of a health club. There is no right or wrong choice in this regard, however, the entity chosen must meet the business requirements of the health club. The options available to the trainers are a partnership or a corporation. Creating a partnership business is relatively inexpensive and easy to start and to manage. In addition, it is suitable for them if they do not consider personal liability a major concern. On the other hand, forming and managing a corporation is complex but it is a good choice for a business that involves high or medium risk. In addition, it is suitable if the partners need to generate finances form a number of investors and have an outlook to carry forward the business in the long-term.

Considering the situation, the health club begins as a small to medium organization. It is highly recommended to the trainers to go for a Limited Liability Company. It is a corporate structure that shares the characteristics of both the partnership business and a company. It not only offers limited liability to the creators of the company and it takes the arrangement of a formal partnership agreement. Setting up an LLC is less complex as compared to a corporation and in case this business form doesn't seem suitable it can be converted to a corporation in later stages.

# Debt vs Equity Financing

If the owners are convinced to form their health club in the form of a corporation, the two most common sources of finance available to them are either from giving a share in ownership or obtaining loans (Dauderis & Annand, 2018). The benefit in case of equity financing is that the investor is also aware of the risks of a business and business can enjoy higher stability since it doesn't have to repay loans. It ensures stable cash flow for business operations and supports its long-term growth. However, it never functions without paying a return to the investors. In addition, the owners will also lose some control over the operations of the club. There can also be a potential for conflict.

The other option available to them is raising funds by borrowing money and the primary advantage of this method is that owners do not have to lose control over business operations. Loans interest is also tax-deductible unlike the profit payments made to shareholders. However, the credit rating is important to obtain loans and it can also disrupt the cash flow of business. More liabilities are not suitable for the success of the company's operations and make it vulnerable to various risks. Both the forms of raising investments has its own benefits and demerits for the health club.

# References

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