- ***Managerial ability.*** Entrepreneurs must assess their own ability to successfully manage their companies. If they lack skill or experience in certain areas, they may need to select a form of ownership that allows them to involve individuals who possess those needed skills or experience in the company.
- ***Business goals.*** The projected size and profitability of the business and any predetermined exit plans influence the form of ownership an entrepreneur chooses. Businesses often evolve into different forms of ownership as they grow, but moving from some formats can be complex and expensive. Legislation may change and make current ownership options no longer attractive.
- ***Management succession plans.*** When choosing a form of ownership, business owners must look ahead to the day when they will pass their companies on to the next generation or to a buyer. Some forms of ownership better facilitate this transition. In other cases, when the owner dies, so does the business.
- ***Cost of formation.*** Some forms of ownership are much more costly and involved to create. Entrepreneurs must weigh the benefits and the costs of the form they choose.
- ***Cost of maintaining.*** In addition to the cost of formation, there are ongoing fees and expenses associated with maintaining a business such as accounting and legal support that can vary based on the form of ownership the entrepreneur chooses.

Business owners can choose from five major forms of ownership: the sole proprietorship, the partnership, the C corporation, the S corporation, and the limited liability company. Social entrepreneurs also have choices in the form of business structure they choose for their ventures. This chapter describes the characteristics, advantages, and disadvantages of these forms of business ownership. Figure 5.1 provides an overview of the various forms of ownership.

The Sole Proprietorship

The **sole proprietorship** is the simplest and most popular form of ownership. This form of business ownership is designed for a business owned and managed by one individual. The sole proprietor is the only owner and ultimate decision maker for the business. Its simplicity and ease of formation makes the sole proprietorship the most popular form of ownership, comprising 72 percent of all businesses in the United States.

2.

Describe the advantages and disadvantages of the sole proprietorship.

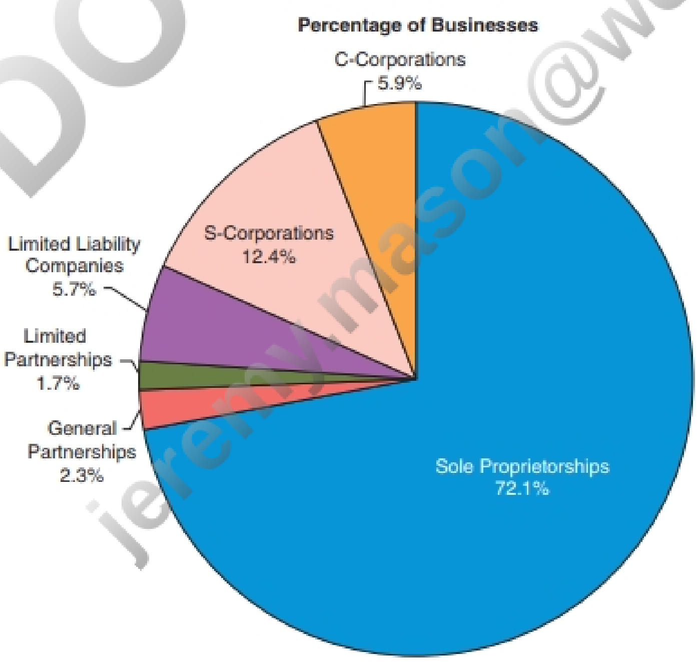

FIGURE 5.1

Forms of Business Ownership

Source: Based on "Number of Returns, Business Receipts, Net Income, and Deficit by Form of Business, Sector Tax Year 2008," Internal Revenue Service, 2012.

Advantages of a Sole Proprietorship

SIMPLE TO CREATE One attractive feature of the sole proprietorship is the ease and speed of its formation. "Sole proprietorships are easy to set up and require very little legal work, outside of a business license," says Jason Deshayes, an Albuquerque-based CPA.[2] For example, if entrepreneurs want to form a business under their own names (J. Jolly Financial Consulting), they simply obtain the necessary business licenses from state, county, and/or local governments and begin operation. In many cases, an entrepreneur can complete all of the necessary steps in a single day because few barriers exist to creating a sole proprietorship. Table 5.2 summarizes the licenses and filings typical for most states and municipalities (specific requirements vary from state to state and city to city).

LEAST COSTLY FORM OF OWNERSHIP TO ESTABLISH In addition to being easy to set up, the sole proprietorship is generally the least expensive form of ownership to establish. There is no need to create and file the legal documents, such as those recommended for partnerships and required for corporations. An entrepreneur, for example, may simply contact the secretary of state's office, select a business name, identify the location, describe the nature of the business, and pay the appropriate fees and license costs. Paying these fees and license costs gives the entrepreneur the right to conduct business in that particular jurisdiction and avoids aggravating penalties.

In many jurisdictions, entrepreneurs planning to conduct business under a trade name are usually required to acquire a Certificate of Doing Business Under an Assumed Name (also known as a Doing Business As or Fictitious Business Name) from the secretary of state. Some sole proprietors use their own names as their company names, such as Bob Smith Towing Service. Others prefer to come up with creative company names as a way of distinguishing themselves in the market and creating the right impression with their target customers.

The fee for the Certificate of Doing Business Under an Assumed Name is usually nominal. Acquiring this certificate involves conducting a search to determine that the name chosen for the business is not already registered as a trademark or service mark with the secretary of state. Filing this certificate also notifies the state of the owners of the business. Additionally, most states now require notice of the trade name to be published in a newspaper serving the trading area of the business.

TABLE 5.2 License and Other Filing Requirements for a Sole Proprietorship

State Requirements	
State business license	Used to track and monitor businesses for tax purposes and are required for businesses to operate lawfully in the state
Tax registration	Required for states with a sales tax
Occupational licenses	Certain professions require practitioners to obtain licenses (doctors, lawyers, accountants, real estate agents, private security guards, funeral directors, private investigators, barbers, and many others)
Local Requirements	
Register business name	Register with county clerk—the default name will be your name, but you can apply for "doing business as"
Local business licenses	License from the local government (city or county) to lawfully operate within their jurisdictions
Zoning permit	Demonstrates that the location of your business is approved by the city or county for your business' usage and can also govern permitted signage, etc.
Health permit	For businesses with food preparation
Building permits	Approval to remodel or build a new space

Source: "State and Local Small Business Licenses for Start-Ups," *FindLaw.com, smallbusiness.findlaw.com/starting-a-business/state-and-local-small-business-licenses-for-start-ups.html.*

PROFIT INCENTIVE One major advantage of operating as a sole proprietorship is that once the owner has paid all of the company's expenses, the entrepreneur keeps the remaining after tax profits. The profit incentive is a powerful one, and, among entrepreneurs, profits represent an excellent way of "keeping score" in the game of the business.

TOTAL DECISION-MAKING AUTHORITY Because sole proprietors are in total control of operations, they can respond quickly to changes. The ability to respond quickly is an asset in a rapidly shifting market, and the freedom to set the company's course of action is both a major motivational and a strategic force. For people who thrive on seeking new opportunities, the freedom of fast, flexible decision making is vital. The entrepreneur solely directs the operations of the business.

NO SPECIAL LEGAL RESTRICTIONS The proprietorship is the least regulated form of business ownership. In a time when government demands for information seem never-ending, this feature has merit.

EASY TO DISCONTINUE If an entrepreneur decides to discontinue operations, he or she can terminate the business quickly, even though he or she will still be personally liable for all of the business's outstanding debts and obligations.

Although these advantages of a proprietorship are extremely attractive to most individuals contemplating starting a new business, it is important to recognize that this form of ownership has some significant disadvantages.

Disadvantages of the Sole Proprietorship

UNLIMITED PERSONAL LIABILITY The greatest disadvantage of a sole proprietorship is the unlimited personal liability of the owner; the sole proprietor is *personally* liable for all business debts. In the eyes of the law, the entrepreneur and the business are one in the same. The proprietor owns all of the business's assets, and if the business fails, creditors can force the sale of those assets to cover its debts. The company's debts are the owner's debts. If unpaid business debts remain, creditors can also force the sale of the proprietor's *personal* assets to cover repayment. State laws vary, but most states require creditors to leave the failed business owner a minimum amount of equity in a home, a car, and some personal items. The reality: *Failure of the business can ruin a sole proprietor financially.*

LIMITED ACCESS TO CAPITAL If the business is to grow and expand, a sole proprietor often needs additional financial resources. However, many proprietors already have invested their available resources into their businesses and may have used their personal assets as collateral on existing loans. Therefore, it may be difficult for sole proprietors to borrow additional funds. A sole proprietorship is limited to whatever capital the owner can contribute and whatever money the owner can borrow. Unless proprietors have substantial personal wealth, they may find it difficult to raise additional money while maintaining sole ownership. Most banks and other lending institutions have well-defined formulas for determining a borrower's eligibility.

LIMITED SKILLS AND ABILITIES A sole proprietor may not possess the full range of skills running a successful business requires. An entrepreneur's education, training, and work experiences may have taught him or her a great deal, yet there are areas in which their decision-making ability will benefit from the insight of others. Many business failures occur because owners lack skill, knowledge, and experience in areas that are vital to business success. Owners may tend to push aside problems they do not understand or do not feel comfortable with in favor of those they can solve more easily. Unfortunately, the problems they set aside seldom solve themselves.

FEELINGS OF ISOLATION Running a business alone allows an entrepreneur maximum flexibility, but it also creates feelings of isolation; there is no one to turn to for help in solving problems or getting feedback on a new idea. Most entrepreneurs report that they sometimes feel alone and frightened when they must make decisions knowing that they have nowhere to turn for advice or guidance. The weight of each critical decision rests solely on the proprietor's shoulders.

LACK OF CONTINUITY FOR THE BUSINESS If the proprietor dies, retires, or becomes incapacitated, the business automatically terminates. Lack of continuity is inherent in a sole proprietorship. Unless a family member or employee can take over, the future of business could be in jeopardy. Because people look for secure employment and the opportunity for advancement, proprietorships often have trouble recruiting and retaining good employees. If no one is trained to run the business, creditors can petition the court to liquidate the assets of the dissolved business to pay outstanding debts.

A sole proprietorship is ideal for entrepreneurs who want to keep their businesses relatively small and simple. Some entrepreneurs, however, find that forming partnerships is one way to overcome the disadvantages of the sole proprietorship. For instance, a person who lacks specific managerial skills or has insufficient access to needed capital can compensate for those weaknesses by forming a partnership with someone who has complementary management skills or money to invest.

Entrepreneurship in Action

What's in a Name?

Clint Smith and Will Weaver were both veterans of the first generation of Internet start-ups. Even though the Internet bubble had burst a year before in 2000, both Clint and Will were confident that there were still opportunities. Realizing that small businesses needed to push out messages to their customers led Clint and Will to think about e-mail as a push-marketing medium. The e-mail services that they had used in previous businesses were not good products for small companies because they were designed for high-volume users and large companies.

They started to work on their new business in early 2002 and decided to name the product Emma. "Basically, EMMA is a quasi acronym for 'Email Marketing,'" says Clint. "There's no Great Aunt Emma, or Grandma Emma, or even Second Cousin Emma who inspired us to create the company. Instead, we chose the name because it was a tangible representation of what we were trying to do conceptually—take a fairly technical product and process and give it all a personable—even human—feel." They tried to secure the domain name emma.com, but it was already reserved by another company. Because they were unable to secure the domain name, they registered the domain name myemma.com instead.

The company experienced significant growth over the next decade, becoming one of the leading companies specializing in e-mail marketing for small business. They branded their product as "emma" and had a registered trademark for "emma" and their "emma" logo. However their domain name remained myemma.com.

MicroStrategy, headquartered in Tysons Corner, Virginia, had purchased the Web domain *www.emma.com* in the 1990s. Emma had approached MicroStrategy on multiple occasions to buy or lease the Web domain. Although MicroStrategy had not been actively using the domain name, Emma was not able to negotiate a deal with MicroStrategy.

In 2011, the conflict over the "emma" name escalated into legal action. Early in 2011, Emma registered with Apple Inc. to create an iPhone app for their e-mail marketing product. However, that same year, MicroStrategy launched its own Facebook products under the "emma" name. MicroStratey's Emma was an app that attaches Facebook credentials to classified listings so that both parties can more thoroughly know about each other when buying or selling merchandise and services. Emma filed a lawsuit claiming that MicroStrategy used the "emma" name in much the same way Emma's own trademark, using lowercase letters and a similar font. The suit claimed that MicroStrategy Inc. intentionally confused Emma's customers and irreparably damaged Emma's business through trademark infringement, trademark dilution, unfair competition, and unjust enrichment. MicroStrategy filed a counterclaim against Emma that claimed that its use of "emma" was not an infringement of Emma's trademark and that both companies should be able to continue to use their trademarks. However, a judge dismissed the counterclaim filed by MicroStrategy.

Internet domain name expert Andrew Allemann observed that Emma's cofounders could have avoided the problem in the first place. "I'm sure the company would prefer to have Emma.com," he said. "But if you don't have it, then you shouldn't brand your company as just 'Emma.' You should brand it as 'MyEmma.'"

1. Is selecting the right name for a business important to its success? Explain.
2. How important is matching a company's name to its domain name? Explain.

Sources: J. Wark and J. Cornwall, "EMMA," United States Association for Small Business and Entrepreneurship, *Proceedings*, 2010; Andrew Allemann, "Identity Crisis: Emma or MyEmma?," *Domain Name Wire*, December 1, 2008, *http://domainnamewire.com/2008/12/01/identity-crisis-emma-or-myemma*; James Nix, "E-Marketer Emma Sues Virginia Firm for Trademark Infringement," *The City Paper*, October 3, 2011, *http://nashvillecitypaper.com/content/city-news/e-marketer-emma-sues-virginia-firm-trademark-infringement*; *http://law.justia.com/cases/federal/district-courts/tennessee/tnmdce/3:2011cv00926/51565/36.*