Gujarat Board Textbook Solutions Class 11 Organization of Commerce and Management Chapter 5 Forms of Business Organisation-1

1. Select the correct alternative and write answers to the following questions :

Question 1. Which is the oldest and easiest form of business enterprise?
(A) Sole proprietorship
(B) Partnership
(C) Co-operative society
(D) Company
Answer:
(A) Sole proprietorship

Question 2. In which form the owner, establisher and manager is only one?
(A) Joint enterprise
(B) Government company
(C) Co-operative society
(D) Sole proprietorship
Answer:
(D) Sole proprietorship

Question 3. The firm of Hindu Undivided Family is managed by whom?
(A) Owner
(B) Karta
(C) Manager
(D) Partner
Answer:
(B) Karta

Question 4. In the firm of Hindu Undivided Family, how one gets the membership?
(A) By agreement
(B) By birth
(C) By investing capital
(D) By managing
Answer:
(B) By birth

Question 5. When did the Indian Partnership Act came in to existence?
(A) 1932
(B) 1956
(C) 1960
(D) 2013

Answer:
(A) 1932

Question 6. What is the minimum number of partners in partnership firm?
(A) 2
(B) 3
(C) 5
(D) 7
Answer:
(A) 2

Question 7. What is the maximum number of members in a banking partnership firm?
(A) 20
(B) 12
(C) 15
(D) 10
Answer:
(D) 10

Question 8. According to Indian Partnership Act the registration of partnership firm is
(A) Compulsory
(B) Not compulsory
(C) Not essential for interest
(D) Not in the interest of the firm
Answer:
(B) Not compulsory

Question 9. Partnership created for doing business with time limit means
(A) Firm with limited liability
(B) Voluntary partnership
(C) Inactive partnership firm
(D) Partnership firm with time limit
Answer:
(D) Partnership firm with time limit

Question 10. The firm, whose life span depends upon the wishes of partners, such firm means __________
(A) Time limit partnership
(B) Voluntary partnership
(C) Nominal partnership
(D) Inactive partnership
Answer:
(B) Voluntary partnership

2. Answer the following questions in one sentence each :

Question 1. Who is called a sole proprietor?
Answer:
A form of business in which the business firm is owned, managed and controlled by only one person is called a sole proprietorship and the person is called proprietor or sole proprietor.

Question 2. How is the liability of owner in sole proprietorship?
Answer:
The liability of the owner of the sole proprietorship is unlimited. This means that he may even have to sell off his personal assets to pay-off the business debts.

Question 3. Who is called Karta?
Answer:
The head of the HUF firm is called the Karta. He is the eldest male member of the family. He administers and controls the entire business; The liability of Karta is unlimited.

Question 4. In Hindu Undevided Family how is the liability of Karta?
Answer:
The other family members can help the Karta in the business activities and provide their suggestions. But they cannot interfere in Karta's works or decisions.

Question 5. How decision are taken in a Partnership firm?
Answer:
At the time of taking an important decision the partners gather and discuss it thoroughly, They share their experience, knowledge and opinions with respect to the decision. When everyone agrees and come to a common conclusion a decision is made. Hence, ...

Question 6. Who manages the Partnership firm?
Answer:
The partners together manage the partnership firm. They may also put the duty of managing on one or few of the partners.

3. Answer the following questions in short :

Question 1. In sole proprietorship, how unlimited liability is harmful to the owner?
Answer:
Unlimited liability:
Sole proprietors cannot free themselves from business liabilities. If their borrowings exceeds their business profits and the proprietors are unable to pay, they will even have to sell their personal assets to repay business debts. In this sense the proprietors have unlimited liability.

Question 2. How is it possible to maintain secrecy in sole proprietorship?
Answer:

- In a sole proprietorship the proprietor does all the business activities himself. He takes care of purchasing, production, developing concepts for sales and . marketing, meeting vendors, customers, etc.
- Since he does all these activities on his own he does not need to discuss his business plans and strategies, skills and ability takes all the decisions and maintains the secrets of the business.

Question 3. What is unlimited liability?
Answer:
The term unlimited liability means that if a businessman is not able to pay the business debts then he will have to sell even his personal assets to pay the debts. Failing to do so the creditors can file a case against the businessman and can take him to the court of law for recovering their money.

Question 4. Give defination of partnership according to partnership Act 1932.
Answer:
According to partnership Act, 1932, "Partnership is a relation between people who have agreed to share the profit of the business which is run by all or one on behalf of all.

Question 5. When can a minor become a partner?
Answer:
If a partner dies than his son who is minor can be made partner.

Question 6. Who is called the partner by Estopple?
Answer:
A person who does not sign the partnership deed, does not bring capital and does not share the profit or loss in the firm but permits himself to be represented as a partner and behaves as a partner is called a partner by holding out or estopple partner.

Question 7. Who is called a nominal partner?
Answer:
A partner who neither invests capital nor plays an active role in management but allows the partnership firm to use his name and influence for increasing the credibility, growth and expansion of the business is called a nominal partner.

Question 8. What is a Partnership deed?
Answer:
A wntten agreement that outlines in detail the rights and responsibilities of each partner for the partnership firm is known as a partnership deed.

4. Answer the following questions in brief :

Question 1. Give the meaning of sole proprietorship and explain the characteristics.
Answer:
Sole proprietorship:

- A form of business in which the business firm is owned, managed and controlled by only one person is called a sole proprietorship and the person is called proprietor or sole proprietor.
- From the above definition one can conclude that a lone trader or a sole proprietor is only and wholly responsible for the entire business and that the entire business is carried out under his direction. He alone enjoys the profit and is responsible for loss in business or insolvency.

Characteristics of proprietorship:
1. Easy to establish:
One can easily set-up a proprietorship business firm without any legal hassles. A proprietor can start his firm from any place he seems proper.

2. Capital:
The proprietor raises his own capital. He can borrow money if he wish but it becomes his sole responsibility to return it.

3. Power of administration:

- The sole proprietor himself looks after the administration. He himself sees purchase, sales, collection, accounting and other business activities.
- However, he may take help from family members, relatives or even hire someone.

4. Freedom of work and quick decisions:
The proprietor enjoys complete freedom as how he wants to run his business. He runs his business based on his intelligence and experience. Since he has all the freedom and no one to interfere he can make quick decisions.

5. Unlimited liability:
The proprietor has unlimited liability. This means that if he is unable to repay his debts, the creditors can claim even for his personal properties and assets in the court of law to recover their money.
In other words if the business incurs loss and the proprietor is unable to pay his debts then he may have to mortgage or even sell his personal assets to repay.

6. Maintenance of secrets:
The proprietor manages everything himself and so his trade secrets do not get leaked.

7. Personal contact:
The reach of a sole proprietorship is generally not very far. Hence, the proprietor is able to maintain personal contact with customer's vendors, etc. This helps him to understand customers, employees, creditors, etc. better, serve them as per their taste, fashion and demand, etc. and keep them satisfied.

8. Centralization of ownership and management:
In sole proprietorship the proprietor is the owner as well as manager. Hence, unlike other business forms there remains unity or say centralization between ownership i.e. owner and management i.e. manager of the business.

Question 2. Give the meaning of partnership firm and list out the characteristics.
Answer:
Partnership firm:

- A business firm run by two or more persons together with the objective of sharing the profit or loss is called a partnership firm.
- According to partnership Act, 1932, "Partnership is a relation between two or more people who have agreed to share the profit and/or loss of the business which is run by all or one on behalf of all".
- In a partnership firm the ownership remains in hands of more than one person or say in the hands of all the partners together. The business is managed by all partners or by one or more partners as per the partnership deed and mutual understanding. Similarly, the profit or loss is borne by all as per the ratio decided in the deed.

Characteristics of partnership firm:
1. Relation by agreement:
A partnership firm comes into existence by either verbal or written agreement called the partnership deed.
It can also come into existence just by mutual agreement and understanding of people, however it is always advisable to have a written agreement.

2. Process of establishment:
The process of establishing is simple and one does not need to undergo a lengthy and complex legal procedure.

3. Registration:
As per the partnership Act it is not compulsory to register a partnership firm but it is advisable to do so. The partners need to submit the partnership deed to the Registrar of Firms who will then register the firm.

4. Number of partners:
A general partnership firm need to have minimum 2 partners and maximum 20. Whereas for a banking business there can be a maximum of 10 partners only.

5. Purpose of partnership firm:

- The main objective of a partnership firm is to earn profit by doing activities that are legally permitted.
- Activities such as social service managing religious programmes or tasks though done together cannot be called partnership because the objective of profit does not exist in such cases.

6. Capital:
Generally, all the partners invest the capital as mentioned in the partnership deed ' however, it is not necessary that every partner invests.

7. Management:
All the partners can jointly manage the partnership firm and all of them can participate in decision making. However, partners can mention and authorize names of one or more partners in the partnership deed who would manage the business.

8. Unlimited liability:
The liability of all the partners is unlimited. This means the partners will have to even sell their personal assets like properties, cars, etc. to pay the business debts. As per the Partnership Act the partners are individually and jointly responsible for paying off the firm's debts. This also means that if one or more partner is unable to pay the business debts from his personal assets, the remaining partners, will have to pay the debt from their personal assets.

9. Transfer of ownership:
It is not easy to transfer the ownership of a partnership firm. Unless all the partners approve one cannot transfer his share in anyone's favour. In case if a partner does so, any partner can dissolve the partnership firm.

10. Legal status:
The Partnership Act, 1932 contains all the details and procedures about registering the firm, rights and duties of partners, establishment, dissolution, etc.

11. Life span of the firm:

- A partnership has a limited life. Partnership and partnership firm exist separately.
- The partnership ends if a partner dies, becomes mentally unstable or insolvent. In such cases, the remaining partners can redistribute the share of that partner among themselves or even admit a new partner. In this way the existing partnership may end but the partnership firm can live, i.e. not get dissolved.

Question 3. 'Sole proprietorship is a training school of business' Explain.
Answer:
Sole proprietorship is the most basic yet fundamentally very important form of business.

- A sole proprietor does all the activities himself or is in direct contact with all those people who conduct business activities on his behalf.
- The proprietor raises his own capital, trades with other businessman, purchases products or raw material, processes them, performs sales and marketing and also manages the books of accounts.
  Moreover, the sole proprietor remains in direct contact with vendors, customers, employees, market, etc.
- All these things are extremely important for a person to understand and do a business. Sole proprietorship teaches the proprietor all these aspects thoroughly and hence it is considered as a training school for business.

Question 4. Each Partner is an agent of other partner – Explain this statement.
Answer:

- For a third party, a partnership firm and partners are one and the same.
- A partner can be looked upon as an agent or say representative of the firm for the business acts he does for the firm or say the partners.
- A partner can thus bind the partners and the firm through his activities and the firm becomes responsible for his acts with the third parties i.e. the outside world. -» Hence, it is said that a partner is an agent of other partners or the firm.

Question 5. Clarify the difference between sole proprietorship and a partnership firm.
Answer:

Point of difference	Sole proprietorship	Partnership firm
Meaning	When a person wishes to establish a business, arranges capital, enjoys the profit and bears the loss all alone it is called a sole proprietorship.	Partnership is a relation between two or more people who have agreed to share the profit and/or loss of the business which is run by all or one on behalf of all.
Number of members in management	Sole proprietorship is managed and controlled by only one member i.e. the proprietor.	A partnership firm can have minimum 2 persons and maximum 10 persons a ban king business and maximum 20 for all other businesses.

Capital	The entire capital is brought in by the proprietor.	Partners bring the capital as per the partnership deed.
Establishment	Anyone can start a proprietorship without any written document/aqreement.	The partners need to establish a partnership either by verbal agreement or written.
Decisions	Since this is run by only one person decision making is fast.	More than one person runs partnership and so decision makinq is slow.
Profit and loss	The owner wholly enjoys the profit or bears the loss.	Profit or loss is distributed among the partners.
Registration	There is no compulsion for registering a proprietorship firm.	Registration is not compulsory but beneficial.
Maintenance of secrecy	The business secrets remain intact with the proprietor.	Business secrets are known to all partners and so secrecy is less.
Transfer of share.	The proprietor can easily transfer his share to anyone whenever he wishes	A partner can transfer his share only if all the other partners agree.
Risk	Only the proprietor bears the business risk.	All the partners bear the business risk.

Question 6. Explain the advantages of registration of a partnership firm.
Answer:
Advantages of registering a partnership firm:

- The partners can file a case and go to the court of law for recovering dues from a third party.
- Any partner can file a case in the court against other partners or the firm.
- A partner can demand justice for his rights and share in the partnership firm from the court of law.
- A partner who wishes to retire from the firm can give a public notice and free himself from his liabilities.
- The existence of the firm becomes known to public through registration.

5. Answer the following questions in detail :

Question 1. State meaning of Hindu Undivided Family and clarify the characteristics.
Answer:
Hindu Undivided Family (HUF) firm:
According to Hindu law business is inheritable. So, a business which is inherited and run by a Hindu Undivided Family is called a Hindu Undivided Family Firm. According to the Hindu law all the male members of the family are considered the members of the HUF firm. The eldest male member of the family administers and controls the entire business. He is called 'Karta'. The eldest male member does not wish to run the business, the administration and control is passed to the second eldest person of the family. HUF firms is quite popular in India and Nepal.

Characteristics of HUF firm:
1. Existence by law:
The concept of HUF firm has emerged from Hindu law i.e. the firm has a legal standing.

2. Management:
The eldest male member manages the HUF firm. This member is called 'Karta'.

3. Independent field of operation:
Kara is free to take all and any business decisions. Other members i.e. family members who are a part of HUF firm can neither involve nor interrupt in decision making. These members cannot object any decision of Karta however they can suggest and help in the business and its decisions.

4. Membership:
Any male member born in HUF automatically becomes the member of the HUF firm from his birth.

5. Financial control:
Since the entire administration and control of business lies with Karta the financial control also lies with him.

6. Liability:
The Karta runs the business, administers it, also controls it fully and hence his liability towards business is unlimited. This means he may have to sell his personal assets to pay off the business debts. Whereas the liability of members is limited.

7. Life of HUF Firm: If the Karta of the HUF firm dies the next eldest person becomes the Karta and this is how the HUF firm remains continued.

8. Difficulty in raising funds: The success of an HUF firm depends on the efficiency of the Karta. The firm depends on the Karta and family members for raising the funds needed to run the business. In such cases since the fund is to be raised by family members only it might be difficult to raise a good amount of capital.

9. Insolvency: In case an HUF firm becomes insolvent the adult members of the HUF firm are declared insolvent whereas the minor members (i.e. bejow 18 years of age) are excluded. The liability of Karta is unlimited while paying the debts. He can sell the shares of all the family members to pay the business debts.

Question 2. Explain the advantages and limitation of sole proprietorship.
Answer:
Advantages of soie proprietorship:
1. Easy establishment process:

- One can easily start a sole proprietorship without any documents or passing from any complex laws and procedures.
- Any person, educated or illiterate but having general capabilities can start a proprietorship with minimal capital.

2. Less capital:
Since the proprietorship can be set up even with very less capital it is a very important characteristic and special advantage. Moreover, in case the business needs more capital, the proprietor can even borrow it.

3. Maintenance of secrets:
It is extremely important for a business to maintain its trade secrets. Since the proprietorship is entirely owned and managed by a single person the business secrets can be very well maintained. This again is a special advantage which is difficult to obtain in other forms of business.

4. Quick decisions:
Since the entire business is owned by a single person quick decisions can be made as per the changes in market, demands consumer preference, etc. Such quick decisions helps to save business and even grow faster.

5. Personal contact:

- The reach of a sole proprietorship is generally not very far. Hence, the proprietor is able to maintain personal contact with customers, vendors, etc. This helps him to understand the customers, employees, creditors, etc. better, serve them as per their taste, fashion and demand, etc. and keep them satisfied.
- Based on the opinions of customers and employees he gathers through personal contact he can even change the product or production method or distribution system, etc. and keep the business safe and sound.

6. Flexibility:
The proprietor can easily bring whatever change he wishes to in his business. Authority to decide solely, quick decision making and constant personal contact makes proprietorship highly flexible to change as required,

7. Less burden of tax:

- The income of sole proprietorship can be considered as the income of the owner. Hence, the proprietor falls into the bracket of personal rate of income tax which is lower than other business forms.
- Moreover, generally the sole proprietorship is not very large and so the burden of income tax is also less.

8. Less legal restrictions:
Compared to other business forms there are lesser regulatory and legal controls on the proprietorship firm. The proprietor does not need to take approval from anyone for making changes in his business methods increase or decrease capital etc. Moreover, since the business is small, regulatory controls are also less.

Limitations of sole proprietorship:
1. Limited capital:

- Generally, it is difficult for a sole proprietorship to raise large capital.
- After industrial revolution and with advent of e-commerce the size of businesses have grown and is growing. In such cases it becomes almost impossible for the owners to raise large capital, large space or purchase machinery, raw materials, etc. in larger quantity. As a result, business may not grow much.

2. Unlimited liability:
Sole proprietors cannot free themselves from business liabilities. If their borrowings exceeds their business profits and the proprietors are unable to pay, they will even have to sell their personal assets to repay business debts. In this sense the proprietors have unlimited liability.

3. Short duration:
If the proprietor becomes insolvent or dies or faces some unforeseen event like loss of mental balance or gets involved in some crime, the existence of business comes in danger. In such situations if there are no inheritors of the proprietors or if they do not possess the knowledge to run the business, the business may become weak or even shut down.

4. Limited capacity to work:

- In proprietorship the owner does everything. He formulates policies, he manages funds, he sells and he markets.

- It is a known fact that an individual has got only 24 hours per day to work and a limited set of skills and preferences towards works. Even if the proprietor is highly efficient he will have limited time and knowledge.
- The sole proprietor may lose out the benefit of skills possessed by other persons, opinions and suggestions, etc. and so the growth of business may be limited.

5. Possibility of wrong decisions:

- All the decisions are taken by the proprietor himself. Hence, he does not have the advantage to take help of rich experience and specialized knowledge possessed by others in their own fields.
- This may result in mistakes in business decisions.

6. Lack of advantages of large scale business:
The proprietorship firm generally works on a smaller scale with limited capital and skills. Under such circumstances the businessman cannot get the advantage of large volume or large scale business to earn large profits.

Question 3. Explain the limitations of partnership firm.
Answer:
Limitations of a partnership firm:
1. Limited capital:

- Considering the growth and development of today's world and the large scale modern industries and trade the capacity of the partners to raise the capital is limited.
- It is difficult for a proprietorship firm to engage in expanding the business on a large scale, investing in research and development, etc.

2. Unlimited liability:
All the partners need to work honestly and efficiently. If a partner does not work properly and the business incurs loss then every partner becomes responsible for paying the debt collectively. Since the partners have unlimited liability, the partners may have to sell their personal assets to repay business debts in case the assets of the firm cannot repay.

3. Possibility of disagreement:
A partnership firm can run successfully and grow well only if all the partners work and think unitedly. If disagreements and disputes crops in among the partners, they may affect the firm too.

4. Difficulty in maintaining secrets:
Important business decisions are taken through discussion and meetings among partners. All the business aspects are discussed in such meetings and so all the partners know all the secrets of the business. As compared with sole proprietorship more than one person knows

the business secrets which in a way can prove dangerous. If any partner leaks them out it may be harmful for the business.

5. Difficulty in transferring the share:
In a partnership firm one cannot easily transfer his share to another person unless remaining all partners agree.

6. Delay in decision making:

- As per the Partnership Act each partner can be a part of management and decision making. If there are disputes or disagreements between the partners the decision making may become poor and delayed. This can then result into weaker management.
- Sometimes disputes differences in opinions and decisions and enmity between partners increase so much that the partnership firm gets dissolved.

7. Short life span:
If any of the partner dies, becomes mentally unstable or insolvent, the partnership comes to an end.

Question 4. State the details to be included in partnership deed.
Answer:
Partnership Deed:
A written agreement that mentions in detail the rights and responsibilities of each partner for the partnership firm is known as a partnership deed.

Details included in a partnership deed:

- Name and address of the firm
- Name, age, address and telephone numbers of each partner
- Purpose of starting the partnership and its duration
- Date of establishing the partnership and its duration
- Details of capital invested by each partner and the interest on capital if it is to be given to the partner
- The limit of money a partner can draw from the business
- Rate of interest on loans given by the partners to the firm
- The ratio of distribution of profit or loss among the partners
- Distribution of work among the partners
- Details of salary or commission of partners or other facilities that the partner can get
- Provision related to keeping the accounts and book-keeping of the firm
- Provision about the power for opening a bank account and power of transactions for each partner
- The method of evaluating the goodwill of the firm
- Provision of involving an intermediary person for solving disputes and differences

- Signing authority for various documents
- Provision of admitting a new partner and retirement of an old
- Rights and duties of a partner
- Provision for admitting a minor partner
- Process of setting the accounts during dissolution of the firm

All the above details are mentioned in the Partnership deed. If the deed is not in a written form then the provisions of Partnership Act 1932 gets automatically applicable to the partnership firm created on the basis of oral agreement.