Business Law

Introduction

Businesses are often referred to as organisations. An organisation is a body that is set up to meet needs. Businesses satisfy these needs by providing people with goods and services. There are many different types of businesses and many different sectors of the market. Each type of business has its own laws and legislation regarding its set up and dissolution.

Sole Trader

The simplest and most common form of private sector business is a Sole Trader. This type of business is owned by just one person and this person will run the business and employ any number of people to help. Examples of Sole Traders could be Farmers, small construction firms, hairdressing, restaurants etc. Most sole traders are in retail and construction, where a very large number of shops and small construction companies are owned by one person. There are more sole traders than any other type of business, however the amount they contribute to the total output in the UK is relatively small.

The setting up of a sole trader is quite simple. There are no legal formalities needed, but sole traders do have a certain amount of legal responsibilities once they are established. Also some types of business may need special permission or licences before they can begin trading examples of these would be the sale of alcohol or a public transport service such as Taxi's. Some of these legal responsibilities include paying income tax and National Insurance contributions. Also once the business has made a certain amount of money they must register for VAT. Planning permission may also be needed in certain locations, and as with every business Sole traders must comply with legislation regarding issues such as healthy and safe working conditions for their employees.

There are many advantages for sole traders, these include: -

- The owner has flexibility to choose their own hours of work, and take holidays when they want to.
- All profit that is made after tax is the owners.
- There is no lengthy process to set up and the admin costs are low.
- Sole traders can offer a personal service to customers mainly because of their size.

There are however a few disadvantages to setting up as a Sole Trader: -

- Sole Traders have unlimited liability and so if the business runs up debts, the owner is responsible for them and may risk losing personal possessions such as your home.
- Raising money can sometimes be difficult as the capital raised is all the owners' money and it is often difficult to arrange a large business loan for one person.
- Sole traders are unincorporated businesses and so can be sued in the event of a dispute.
- Illness could cause a problem especially if the business has few or no employees.

Finance for a Sole Trader

A sole trader may find it more difficult to raise the necessary finance as they are doing it alone whereas with a partnership the capital that needs raising can be shared between a number of people. Arranging a long-term loan with a bank is often limited and the bank is likely to ask for a certain amount of security on the loan, which may be land, or property of the owner. If the business were to accrue debts then the owner is fully responsible for these and so they would risk losing their house and /or property. Another problem with the limitations on bank loans is that expansion is usually only possible through ploughing the profits of the business back into it

The funds can come from a number of sources:

1. Personal savings of the owner could be used. The owner may have been saving for a number of years with an aim to setting up their own business, another source may be redundancy money which the owner may have got from leaving a firm.
2. Start up costs can be made easier by trade credit. The owner can buy all the necessary equipment or materials on credit and pay over a certain amount of time with interest. The owner will need to be careful to ensure that he can meet all the payment dates so as not to run up business debts. Alternatively for the first few years of trading the owner could lease the necessary equipment until the business is making enough money to make these purchases.
3. Banks offer loans and overdraft facilities for people who wish to set up a business. Banks will ask for security, which could be property, and they will need to see a business plan.
4. In some cases a sole trader may be able to get some government funds. The government also runs a small firms loan scheme where people with no history of trading or borrowing can borrow money. Government funds are available for businesses setting up in certain areas in the country.

Dissolution of a Sole Trader.

The dissolution of a Sole Trader is quite simple, the business will come to an end either when the owner dies or when the owner stops trading completely.

Partnerships

The Partnership Act, 1890, describes a partnership the ***'Relation which subsists between persons carrying on business with a common view to profit'*** Source Nutshells Law, Sweet & Maxwell.

A partnership consists of more than one owner. The owners will share the responsibility of running the business and the profits of the business. Often with partnerships the partners will specialise, for example with an Solicitors firm, you may find that each partner will specialise in a different area for example civil law, family law, criminal law etc.

There are no legal requirements when a partnership is formed but it is common for partners to draw up a *Deed of Partnership*. This is a legal document, which covers each of the partners' rights, so that it can be used in the event of a dispute.

The deed of partnership will include issues such as the amount of capital that each owner will contribute to the business. Also it will have rules for taking on new partners, how much control that each partner has, and how the profits will be shared amongst the partners. There are times when partnerships did not draw up a deed of partnership. In this case if a dispute was to arise then the arrangement between partners will be decided according to the Partnership Act. For example if there was a dispute about the sharing out of profits then the Act states that all profits should be shared equally amongst all the partners.

The Advantages of a Partnership include:-

- More finance can be raised, as there is more than one owner.
- Each partner can specialise, which could improve the running of the business.
- May be easier to raise finance from banks and other institutes as it will be smaller amounts from each partner rather than one lump sum from a sole trader.
- Partners can share the workload, and can cover each other for holiday and sickness. Also when key decisions are being made they can exchange ideas and opinions.
- There are no legal formalities when setting up the business.

However as with every type of business there are disadvantages to a Partnership these include:-

- Each partner has unlimited liability and so each partner will be equally liable for debts.
- The size of a partnership is limited to 20 partners, and so there is a limit on the amount of money that can be raised.
- Profits have to be shared equally amongst all partners
- Partners could disagree on decisions which could lead to disputes and difficulty in decision making for example one partner may wish to retain more profit and another may wish to retain less.
- They have unincorporated status and can be sued by customers.
- Any decision made by one partner on behalf of the company is legally binding for example if one partner agreed to buying a van, the other partners must honour this.

Raising finance for Partnerships

The main source of finance for a partnership comes from the owners. A partnership can obtain finance from all partners, even if some are not actively involved in the business. Bank loans, or personal savings are likely to be the main source of finance for each partner. As with sole traders, the partnership may decide to purchase its equipment or machinery on credit or rent it until they have sufficient capital to buy it. Business angel's offer firms a source of financier, they are individuals who invest money in business start-ups.

Dissolution of A Partnership

A partnership will end when one of the partners dies. The partnership must be wound up so that the partner's family can retrieve money invested in the business. It is normal for the remaining partners to form a new partnership shortly afterwards. There are many other circumstances in which a partnership can come to an end these can be seen in Appendix 2 – The Dissolution of a company.

Companies

There are many types of Limited companies in the UK. One feature is that they all have a separate legal identity from their owners. This means that they can own assets, form contracts, employ people, sue and be sued in their own right. Another feature is that all their owners have limited liability, and so if a company has debts, an owner can only lose the money that they invested. They cannot be forced to use their own money to pay debts like sole traders and partnerships, and whereas partnerships and sole traders pay income tax on profits, limited companies pay corporation tax.

The capital of a limited company is divided into shares, and each shareholder owns a number of these. The shareholders are the joint owners of the company and can vote and take a share of the profit. Those with more shares will have more control and can take more profit. Limited companies are run by directors who are appointed by the shareholders. The board of directors, which is headed by a chairperson, is accountable to shareholders and should run the company as the shareholders wish. If the company does not perform well the shareholders can vote out a director at an annual general meeting (AGM).

ROLE OF DIRECTORS

Soletraders:- This type of business is owned and run by one person who may employ as many people as he needs. He will then be the owner/manager/director of the company unless his business grows and he wishes to appoint a person as a director for his company. Owner is in complete control and is free to make any decisions.

Partnerships:- Usually there are between 2 and twenty partners. These will all have a role in the running of the business and so there may be no directors but the partners will run the business and manage each side i.e. finance according to the partners specialist skills. The authority of an individual partner will vary depending on whether the firm is commercial or non-commercial.

There is no need for directors in the above cases as they are not likely to hold board meetings and any meetings that are held the decisions will be made by the owner or the partners.

Private Limited:- these may have only one director but the sole director cannot also be the company secretary. Generally the members nominate directors, however the director need not be a member himself. Directors can resign and may also be removed from office by an ordinary resolution of members usually at the AGM. Any person may be disqualified from being a director under the Company Directors Disqualification Act 1986. A director must act in the interests of the company and if he makes any profit from his position he may be required to account for it to the company. Any loans made to directors and the terms of the director's contracts must all be disclosed.

Public Limited Company: - Huge amounts of money is made from the sale of shares to public and so the public make up the majority of shareholders and attendees of AGM's and consequently decisions made at AGM and resolutions formed for AGM. Everything is the same as above except public limited companies must have more than one director.

The Formation of A Limited Company

Limited companies must produce two documents – The Memorandum of Association and Articles of Association. The memorandum sets out the constitution and gives details about the company. The Companies Act 1985 states that it must include the name of the company, the name and address of the companies registered office, the objectives of the company and its scope of activities and the liability of its members. It should also include the liability of its members and the amount of capital to be raised and the number of shares to be issued.

A limited company must have at least 2 members. The Articles of Association deal with the internal running of the business this should ideally include items such as the length of time that a director should serve before re-election, the arrangements for the audit of company accounts, the procedures for appointing directors and the timing and frequency of company meetings.
(See appendix 4)
A statement indicating the names of the directors along with these two articles should be sent to the Registrar of companies. If successful a business will receive a Certificate of Incorporation which will allow it to trade. All shareholders have the legal right to attend the AGM and should be told of the date and venue in writing well in advance.

Meetings
Sole Traders and Partnerships will run their businesses differently to a company and the way in which they conduct their meetings will differ in the way that companies meetings are often large scale meetings including the shareholders whereas with the other businesses meetings will often be just a formality to check the running of the business and to discuss any issues if and when they arise. The Table below summarises the differences between the type of business and the meetings that they hold.

Business	Meeting
SOLE TRADER	May have no need to hold meetings depending on whether or not he employs any staff in which case he may hold a meeting. May also have meetings with people external to the business ie the bank.
PARTNERSHIP	Meetings are likely to be held regularly with the majority of partners attending so that each partner is aware of the companies progress and (if any) problems. May also have meetings in separate departments depending on the size of the company. If there are different departments it is likely that a partner will be a manager of these depending on their specialist skills.

PRIVATE LIMITED COMPANY	Must hold AGM each year- directors will call this meeting and sufficient notice must be given to attendees. Directors can also hold an EGM if they require- not statutory that they do. A member of the company who owns shares can appoint a proxy to attend and vote for him for private limited companies you can only appoint one but this person can speak at the meeting voting can be by poll or show of hands.
PUBLIC LIMITED COMPANY	Must hold AGM each year- directors will call this meeting and sufficient notice must be given to attendees. Directors can also hold an EGM if they require- not statutory that they do. Director will decide which resolutions are included in the notice of a meeting, can also exclude a resolution unless a large amount of people force its inclusion. Can appoint more than one proxy but they cannot speak at meeting. Voting can be by poll or show of hands.

Private Limited Companies

These types of businesses tend to be relatively smaller. Their name ends in Limited or Ltd, and shares can only be transferred ‘privately’ and all shareholders must agree on the transfer. The shares cannot be advertised for general sale. Private limited businesses are often family run and the directors of these firms tend to be shareholders and are involved in the running of the business.

The advantages of this type of business are: -

- The business will continue even if one of the owners dies. The owner’s shares will be transferred to another owner.
- More capital can be raised, as there is no limit on the number of shareholders.
- Control of the company is not lost to outsiders. Shares are only sold to new members if all owners agree.
- Shareholders have limited liability and so are more prepared to risk their money as their personal possessions are not at risk.

The disadvantages of this type of business are: -

- Usually profits will have to be shared out to a larger amount of members
- There is a lengthy and costly legal procedure to setting up the business.

- Financial information can be inspected by any member of public. Competitors will often use this to their advantage.
- Firms cannot sell shares to the public and so this restricts the amount of capital that can be raised.
- If a shareholder sells his shares it can sometimes be difficult to find a new buyer.

Dissolution of a Private limited Company

The dissolution of a Private Limited Company is much the same as a Public Limited company the details of these can be seen in the table in appendix 2.

The dissolution of companies (see appendix 2)

Public Limited Companies

These tend to be larger than private limited and the name ends in plc. Public limited companies make up a very small portion of businesses in the UK, however they contribute the more to national output and employ far more people than other types of business. The shares of these companies can be bought and sold on the stock exchange. Once the company has been issued with its Certificate of Incorporation (which it will get by completing the memorandum of association, articles of association and a statutory declaration) it is usual to issue a prospectus. This is a document, which advertises the company to potential investors and invites them to buy shares before they float them on the stock exchange.

Forming a public limited company can be very expensive. The company needs lawyers to ensure that their prospectus is legally correct and a large amount of glossy publications will need to be produced. Also the company must have a minimum of £50,000 share capital. The share issue has to be underwritten and a fee is paid to an underwriter who must buy any unsold shares.

With public limited companies the general public must hold at least 25% of shares and usually there should be a minimum of a £1 million market valuation before it is listed on the stock exchange.

Many of the advantages are the same as those for private limited companies. For example, all members have limited liability, and the firm will continue to trade if one of the owners dies. Others are as follows:-

- Huge amounts of money can be raised from the sale of shares
- Plc's can usually dominate the market because of their size.
- It is easier to raise finance as financial institutions are more willing to lend to plc's.
- Productions costs can be lower as firms may gain economies of scale.

The disadvantages of a public limited company include: -

- The setting up costs can be very expensive sometimes running into millions
- Because of their size it makes them less able to deal with customers personally.
- All of the accounts can be inspected by the public and competitors may use this information to their advantage as they have to publish more information than private limited companies.

- The way they conduct their business is controlled by various company acts which aim to protect shareholders.

There is a vast difference between the organisational structure of a public limited company and other companies. The difference between the business org can be seen in the table in appendix 1.

Types of Shareholders

There are many different types of shareholders that can be involved in a business these include:-

- Directors – directors are elected by shareholders each year and they are responsible for running the business. They do not have to hold shares in the business but generally they do.
- Managers – these are usually appointed by directors and are actively involved in running the business. Sometimes they are allowed to buy shares or given some as a bonus. It is argued that if managers hold a share in the company it might motivate them to perform well in their job.
- Employees – as with managers some companies offer shares to staff as an incentive or bonus and a large number of people will own shares as they are part of the general public.
- Individuals - with public limited companies they must ensure that at least 25% of their shares are bought by the public, and so individuals hold a large amount of shares.
- Investors – these are financial institutions such as insurance companies who buy shares to earn income. They buy and sell large numbers of shares but rarely take part in the running of the business.
- Other companies – some firms hold shares to control other companies and to build up stakes in companies with a view to taking them over in the future.

These four types of business operate very differently and although some may have similar objectives they have to run their businesses in a way, which the legal regulations determine, and in a way that incorporates their target market and environment.