

The Artist as Entrepreneur

Getting Down to Business: Get Organized

Lesson Description

In this lesson, students will take the final step in writing their business description by examining the different forms of business structure and choosing the one that is appropriate for their business.

Concepts

Sole proprietorship
Partnership
Limited liability company
Corporation

Related Subject Areas

business

Objectives

Students will:

state the advantages and disadvantages of various business structures
determine a business structure for their businesses
complete their business descriptions

Materials

Visual 1, *Good News, Bad News*
Visual 2, *Nip it in the Bud*

Procedures

1. Explain that for many, the production of art is a singular activity. This is particularly true in the fine arts, media arts, and craft arts. In this case, the artist is considered a sole proprietor. However, in areas of public and performance art, artists often collaborate. These collaborations can be organized as for-profit companies or not-for-profit companies, depending on the mission of the collaborative. For example, if the collaborative is formed for the purpose of advocacy or activism, it is likely a not-for-profit. In this class, the focus will be on for-profit businesses.
2. Explain that there are four general types of business organization: sole proprietorship, partnership, limited liability company, and corporation. Artists can be organized as any of these. The type of organization the artist chooses will make a difference in how his or her business pays taxes and keeps records.

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3. Explain that the sole proprietorship is a type of organization where an individual or married couple operates their own business. Display Visual 1, *Good News, Bad News*, and discuss the advantages and disadvantages of organizing as a sole proprietorship, as follows.

Good News

All decisions are the responsibility of the sole proprietor. If the sole proprietor is inept, this could be bad news. However, entrepreneurs tend to be independent, and artists tend to be independent. Put the two together, and you have someone who wants to make his or her own decisions and operate as his or her own boss.

Sole proprietorships are cheap to organize. The business owner usually must register the name of the business with the Secretary of State's office. This is called a "fictitious name" registration because most businesses decide on a name that describes the nature of the business or is appealing and unique. For example, a business that is run by John Smith and operates under the name John Smith's Art does not have to register as a fictitious name; however, a business that is run by John Smith and operates under the name Smith's Art or The Artsmith must register. Registering is an easy, do-it-yourself process. No lawyer required.

It is relatively easy to file taxes. The artist, as a sole proprietor, reports business income and expenses on a separate form and attaches it to his or her personal income tax report. So, filing business taxes is only as difficult as filing personal taxes.

Bad News

Sole proprietors face unlimited liability. A person in business as a sole proprietorship is personally liable for business decisions or acts of negligence that result in a financial judgment against him or her. This means that the person who is suing for damages can get the assets of the business, such as the cash, equipment and materials, but can also get the personal assets owned by the sole proprietor, such as his or her personal cash, car, and house. When people choose to organize in a way other than as a sole proprietor, this is the reason.

4. Explain that a partnership is two or more people forming a business. They must complete a partnership agreement that defines the business's management and operation. There are different types of partnership. In a general partnership, two or more people are involved in operating the business. In a limited partnership, the limited partner is not involved in the day-to-day business operations. Usually, he or she is the partner with the money.
5. Explain that collaboration is common among artists. Such collaborations are not necessarily formal partnership agreements. When working on projects with other artists, it is important to precede the work with a discussion covering potential

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conflicts. If two or more artists of forming a formal partnership, this is especially important and foreseeable conflicts should be resolved and placed in the partnership agreement.

6. Display Visual 2, *Nip it in the Bud*. Address each issue as follows. Possible areas of disagreement are shown in italics.

Who will be responsible for various tasks? *It's one thing to do the creative work but quite another to clean tools, take orders, pack and ship, and perform other menial tasks.*

If one of the partners proposes a project that generates little interest among the other partners, can that partner proceed with the idea on her own? *A partner may be passionate about a project and frustrated by the lack of support within the group. Should the partner be allowed to proceed on her own time? How much time must each partner devote to group projects?*

How are the costs of doing business to be divided? How are the profits to be shared? *One partner may have the ability to provide greater financial resources to the group. This partner could take a larger share of the profits or could be excused from certain menial tasks. The partners should make these decisions prior to entering into a project or partnership.*

What business decisions must be discussed before those decisions are made? Are partners free to enter into contracts without consulting the group? *Some decisions are so trivial that requiring joint agreements would be unproductive. However, some decisions, if made improperly, could harm the business and, in the case of a formal partnership, could put all partners at risk of losing personal assets. For example, deciding on which long distance service to use may be a decision left to just one partner. However, if two partners sign contracts that commit the partnership to labor-intensive projects, one of those projects may not be completed on time. This could present the partnership with legal problems.*

7. Explain the advantages and disadvantages of forming a business as a partnership.

Good News

Partnerships are easy to organize. Partners simply send the Fictitious Name Registration to the state Secretary of State's Office and complete a partnership agreement outlining the duties and financial obligations of the partners.

It is relatively easy to file taxes. Each partner's share of the company's profit is reported on that partner's individual tax return.

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Bad News

Sometimes partners don't get along. It's impossible to agree on everything, but sometimes the disagreements become so pronounced or constant that the partnership must be dissolved. This could be particularly true of artists who may have creative differences. When the partnership is dissolved, the business is dissolved, until someone picks up the pieces and reorganizes the business.

Partners face unlimited liability. This is particularly bad with partnerships because each partner is responsible for the activities of the other partners. So, one partner may have to pay for the mistakes of another partner.

8. Explain that a limited liability company is a new form of organization that combines features of corporations, partnerships, and sole proprietorships.
9. Explain the advantages and disadvantages a limited liability company.

Good News

Limited liability companies offer (you guessed it) limited liability. This means that none of the personal assets of the business owners are at risk. There is an exception to this. If someone in business engages in illegal behavior that causes damage to a customer, supplier, or other entity, the offender's personal assets would be at risk.

The owners of a limited liability company are taxed like sole proprietors. They pay according to their level of income – just like the rest of us.

Bad News

Limited liability companies are costly to form. Creating a limited liability company generally requires the assistance of a lawyer.

10. Explain that corporations are very different from the other types of business organizations. They are separate legal entities. This means that corporations are separate from their owners. If the owner of a sole proprietorship or one of the owners of a partnership quits the business, the business is dissolved. However, if an owner, called a shareholder, of a corporation quits by selling his or her stock, the corporation goes on. Corporations can live forever.
11. Explain that there are advantages and disadvantages to forming a corporation.

Good News

Corporations offer limited liability. If a corporation gets sued or goes bankrupt,

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shareholders could lose all of their investment, but they would not lose any personal assets.

Bad News

Corporations are costly to form. Anyone setting up a business as a corporation had better get a lawyer. Articles of Incorporation must be filed with a state government. Separate tax forms are submitted to the Internal Revenue Service.

12. Explain that artists are likely to be operating a sole proprietorship unless their product has the potential to harm someone. For example, the owner of a dance troupe must hire dancers. If a dancer were to be injured during a performance, the owner of the troupe could likely be brought into a lawsuit. For this reason, the owner of the troupe might choose to be incorporated so that only the assets of the business would be in jeopardy. An alternative plan would be organize as a sole proprietorship and carry a large liability insurance policy.
13. Instruct students to consider the following businesses to determine a business structure that may be most appropriate. Students should justify their answers.

You operate a small gallery where you show your own work and show the work of others on consignment. *(limited liability company or corporation – there is a risk of damage to other's work)*

You have joined with a fellow artist to create publicity materials for a local band. *(sole proprietorship – it would be wise to work out potential problems in advance and in writing. This is not a long-term relationship so there is no need to enter into a partnership agreement. There is little risk of liability for harm to someone or for breach of contract)*

You have joined with a fellow artist to form a business offering computer-generated graphic art. *(partnership – this is a long-term relationship. There is little risk of harm to others)*

Closure

Instruct students to add a brief statement to the business description defining their business structure. Ask students to explain their choice.

Explain that they have completed the business description component of their business plans. Ask if this examination of their businesses have caused any of them to reconsider their five- or ten-year goal statements.

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Visual 1

Good News, Bad News

Sole Proprietorships

Good News

- Easily organized
- Allows independent business activity
- Ease in reporting taxes

Bad News

- Unlimited liability

Partnerships

Good News

- Easily organized (although somewhat more complex than a sole proprietorship)
- Allows specialization
- Ease in reporting taxes

Bad News

- Unlimited liability
- Chance for disagreements

Limited Liability Companies

Good News

- Limited liability
- Ease in reporting taxes

Bad News

- More complex to organize than sole proprietorships or partnerships

Corporations

Good News

- Limited liability

Bad News

- Costly to form

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Visual 2

Nip it in the Bud

When two or more artists decide to work on a joint project, it is imperative that they consider the many areas where they might likely have disagreements and work toward a “meeting of the minds” before their work begins. This is important for those who are involved in a one-time collaboration and it is important for those who are planning to form a partnership.

The following are just a few questions to address.

- ◆ Who will be responsible for various tasks? It’s one thing to do the creative work but quite another to clean tools, take orders, pack and ship, and perform other menial tasks.
- ◆ If one of the partners proposes a project that generates little interest among the other partners, can that partner proceed with the idea on her own?
- ◆ How are the costs of doing business to be divided? How are the profits to be shared?
- ◆ What business decisions must be discussed before those decisions are made? Are partners free to enter into contracts without consulting the group?