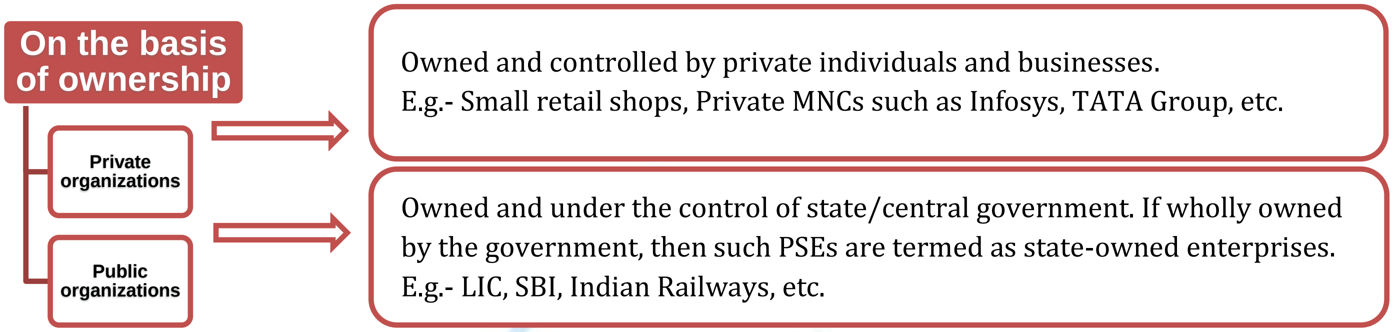
The chapter starts with the classification of business organizations based on the *ownership* and *profitability*.

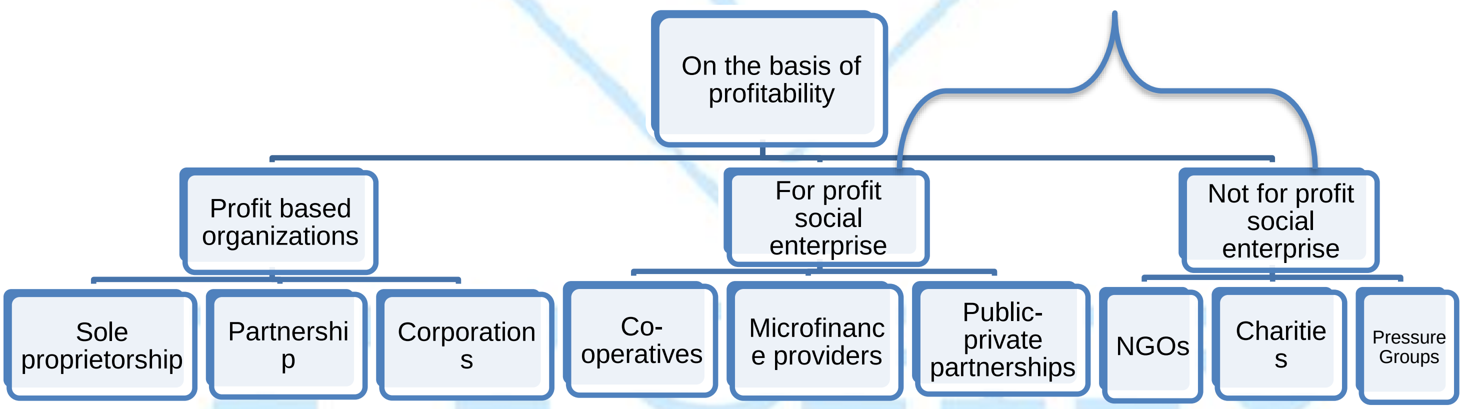


Why do you think public sector businesses are required?

Well, many reasons can justify the importance of public sector in an economy. The outlines are listed below:

- These businesses ensure the access of basic public utility services such as education, healthcare, transportation, libraries, etc. to everyone at affordable rates.
- To avoid wasteful competition.
- To stabilize the economy and protect it from financial crisis.
- To create mass employment opportunities.

Social enterprises are revenue-generating businesses with social objectives at the core of their operations. Social enterprises operate as both for-profit social enterprises and non-for-profit social enterprises. They have two main goals: To achieve social objectives and to earn revenue in excess of



Profit- based organizations- Businesses that aim to make profit. Most of the private sector firms aim for profit maximization.

For profit social enterprises- These are revenue generating enterprises which aim for maximizing social impact along with the profits.

Non- profit social enterprises- These are the commercial enterprises which use their surplus revenues to achieve social goals. Their inclination is towards society rather than profit making for owners.

Sole proprietorship

- Any profit-making enterprise that is owned and run by a single person (sole proprietor).
- It has no separate legal existence from that of its owner.

- The liability of sole proprietor is unlimited, which means the personal property of trader can be sold off to meet his financial obligations. Examples of sole trader: **Freelance writer**, **tutor**, **local vendor**, etc.

Advantages of sole proprietorship	Disadvantages of sole proprietorship
Low Startup cost – Very few legal formalities are involved in setting up a sole proprietorship firm.	Sole traders have unlimited liability i.e. their personal assets have to be sold off in case of financial loss.
Sole trader is the only owner and takes all the profits home.	High risk- The losses have to be borne solely by the trader, if any.
Sole trader is his only boss and takes all the decisions related to enterprise.	Sole trader has to take the responsibility for ownership as well as the management of the firm. The workload causes stress.
Sole proprietorship firms enjoy privacy because they do not have to share their financial statements with the public.	The sources of finance are limited for sole proprietorship firms. They cannot raise money by issuing shares, unlike public limited companies.

Partnership

- A profit-making business owned together by 2 or more individuals.
- There must be minimum of **2 persons** to start a partnership firm. Maximum- 10 in case of banking business and 20 in case of any other business.
- Just like sole proprietorship, partners in a partnership firm also have unlimited liability.
- It is not compulsory to get the partnership firm registered under The Partnership Act, 1932, but unregistered firm gets deprived of few benefits, so the partners consider it a better option to get the firm registered.
- There is a legal agreement among the partners known as **"partnership deed"** which specifies the terms of contract such as **profit/loss sharing ratio, capital contribution ratio, names and details of the partners, duties and responsibilities of all the partners, etc.**
- The profits/losses generated are shared among the partners in an agreed ratio.
- There is no separate legal existence of partnership firm from its owners. The firm implies the collective partners.
- The firm gets dissolved with death, lunacy, or bankruptcy of any partner, but the rest of the partners can choose to continue with a new agreement.

Advantages of partnership	Disadvantages of partnership
There is increased financial strength due to investment done by several partners and the availability of external sources of finance.	Partners in a partnership firm have unlimited liability.
The responsibilities and workload are equally shared by the partners.	Disagreements and conflicts are most common in partnerships among the partners.

The presence of more than one individual in a business brings in more creativity and innovation.	There is delay in decision making because there are many owners involved.
Partnerships are not liable to share their financial statements with the public, just like sole proprietorship.	The partnership comes to an end on lunacy, bankruptcy, or death of any partner and thus the continuity breaks.

- Apart from general partnerships, there are **LLPs (Limited liability partnerships)** where the liability of some or all the partners is limited to the capital contributed by them.

EXAM TIP:
Sole traders and partners have unlimited liability so that they do not take any careless decision while managing the business and remains accountable for their actions and decisions.

Corporations

- A corporation is separate legal entity distinct from its owners.
- The shareholders and the promoters of the company are its owners.
- The liability of shareholders is limited to the extent of their share of investment in the company.
- The corporation continues to even after the death/bankruptcy of any owner/director since the ownership is transferable.
- **Board of directors (BOD)** are elected by the shareholders of the company to manage the company and represent the company on their behalf. They are accountable to shareholders for the performance and activities in a company.

Limited liability companies

Private limited companies

A private limited company is the one that cannot raise capital from the public. The company is not publicly traded on stock exchange rather the shares are sold to family members and friends.
Private limited companies have word **'Limited'** or the letters **'Ltd.'** written after their company's name.
Examples- PricewaterhouseCoopers Pvt. Ltd., Marriott hotels India Pvt.

Public limited companies

On the other hand, a public limited company is listed publicly on stock exchange, for the shares to be purchased by public. These companies generally carry the letters **'PLC'** or **Inc. (incorporated)** after their name, but it varies from country to country.
Example- Coca Cola, HSBC, etc.

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Steps in the formation of a company in brief:

Promotion stage

Incorporation stage

Capital subscription stage

Commencement of business

a) PROMOTION

According to Guthman and Dougal, "Promotion starts with the conception of the idea from which the business is to evolve and continues down to the point at which business is fully ready to begin the operations in a going concern."

The individual/individuals involved in promotion are called **'promoters'**.

b) INCORPORATION

The promoter, before getting the company registered, takes the decisions related to name of the company, location of its registered office, amount of share capital.

The following documents are then filed with the **registrar of companies**:

- **Memorandum of Association (MOA)**
- **Articles of Association (AOA)**

It is the document which contains all the fundamental details pertaining to a company, such as the name, location, purpose, amount of share capital, etc.

It is longer than MOA and outlines all the internal regulations and the procedures of the company. E.g.- Rights and duties of BOD and shareholders, appointment process of BOD, procedures of conducting AGM (Annual General Meeting), etc.

- **List of directors**
- **Written consent of directors**
- **Statutory declaration**

Once these documents are filed with the registrar and the applicable fees is paid, the details are duly verified by registrar. Finally, a certificate of incorporation is issued to the company and the company gets registered under the Companies Act. This provides the license to the company to operate as a separate legal entity.

c) CAPITAL SUBSCRIPTION

A prospectus is drafted and filed with the registrar. The prospectus is circulated, and public offer is made for subscription and the shares are listed on stock exchange.

d) COMMENCEMENT OF BUSINESS

A *private company* can commence its business soon after receiving the certificate of incorporation.

But a public company can commence its business only after receiving the **'certificate of commencement of business'**. Once, the shares are issued, after the sale of shares, the company sends the documents including bank letter are sent to the registrar stating that application money for shares has been received, once the documents are scrutinized and verified, the registrar issues the certificate of commencement of business.

Advantages of limited companies	Disadvantages of limited companies
Large amounts of funds can be raised by the issue of shares.	There is high compliance cost associated with the corporation.
The company's promoters and shareholders have limited liability.	The financial statements of the company must be provided to the shareholders. Hence privacy does not exist in corporations.
The corporations are larger in size when compared to sole proprietorship and partnerships. This gives the companies the benefit of economies of scale.	Unlike sole proprietorship and partnership, companies face the threat of hostile takeover.
Unlike partnerships and proprietorships, the corporation continues to exist even if there is any change in the existence of owners.	There are lot of complexities and bureaucracies involved in running a corporation as compared to a sole proprietorship/ partnership.

Difference between private limited companies and public limited companies

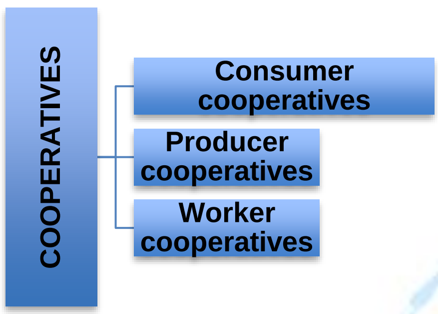
Main points of difference	Private limited companies	Public limited companies
• **Share capital**	A private limited company cannot raise capital from the public by listing the shares on stock exchange.	A public limited company's shares can be purchased by the public. The primary motive of public sector businesses is public welfare.
• **Company's name**	Private limited companies have word **'Limited'** or the letters **'Ltd.'** written after their company's name.	These companies generally carry the letters **'PLC'** or **Inc. (incorporated)** after their name, but it varies from country to country.
• **Commencement of business**	A private company can commence its business soon after receiving the **certificate of incorporation**.	But a public company can commence its business only after receiving the **'certificate of commencement of business'**.
• **Minimum number of members**	The private limited company can be started with a minimum of two members.	The minimum number of members required to start a public company is seven.
• **Statutory general meeting**	There is no compulsion for a statutory general meeting in case of a private company.	In case of a public company, it is compulsory to call a statutory general meeting of members.

Have you heard of the term IPO before? I am sure you may have if you check on the stock market. When the shares of a public limited company are listed for the first time on stock exchange, for the shares to be offered to public/ external shareholders, it is called **IPO** or **"flotation"**.

For-profit social enterprises:

a) **Co-operatives**

Cooperatives are those social enterprises which are private, owned and controlled by the people who use its products. The members of a cooperative society (employees, customers) work together and act in a socially responsible way to create value for all. Any profit earned is shared among the members. The concept of cooperatives began after *Industrial revolution.* Cooperatives operate in various industries such as child-care services, agriculture, wholesaling and retailing, utility services industry, etc.
Some good examples of cooperatives are-**Amul**, **IFFCO (Indian Farmers Fertilizer Cooperative Limited)**, etc.



Consumer cooperatives: These are owned by customers who buy the goods/services for personal use. E.g.- credit unions, health-care cooperatives
Producer cooperatives: Cooperatives that join to support each other in production or marketing.
Worker cooperatives: Cooperatives set up and owned by workers/employees. E.g.- A farmer cooperative.

Advantages of cooperatives	Disadvantages of cooperatives
Employees get an incentive to work since they have a key stake in the performance of cooperative.	Financial incentives are too low. This reduces the efficiency of employees and managers.
Employees have decision-making power. This boosts their motivation.	The sources of finance are limited to the capital contribution of the members.
Cooperatives create social gains that can be enjoyed by the wider community.	Democratic form of decision-making slows down the process in cooperatives.
Since cooperatives work for social benefit, they tend to receive public support.	Cooperatives have flatter organizational structures. This limits the promotion opportunities for employees.

b) **Micro finance providers**

These social enterprises which provide financial solutions to low income and deprived population to uplift them, especially women. This helps in promoting the small enterprises and foster economic growth.
Example- **Grameen Bank** (Bangladesh), **Annapurna Microfinance Ltd.** (India), etc.

Advantages of micro-finance providers	Disadvantages of micro-finance providers
They provide finances to entrepreneurs of small businesses and make them financially independent.	MFPs provide small amounts of money to the borrowers considering the high risk of default.
These social enterprises help in creation of job opportunities.	Not all the low-income individuals are able to meet the eligibility criteria of micro-finance providers.

c) Public-private partnerships

A profit making social enterprise formed with the partnership of government and a private sector enterprise to jointly provide certain goods/services. Examples- **WHO**, **Hongkong Disneyland**, **Mumbai Metro**, etc.

3 types of PPP:

- **Government funded PPPs** - In such ventures, the funding is wholly done by the government, but the management lies in the hands of private business in partnership.
- **Private funded PPPs**- On the contrary, in such PPPs, the funding is in the hands of private sector while the government is liable to manage the enterprise projects.
- **Government directed but with private sector finance and management-** It involves both funding and management done by private business for the public projects based on government specifications. Such projects are leased back to the government.

Advantages of PPPs	Disadvantages of PPPs
The risks are spread/ diversified among the private sector organization and the government.	Huge amounts are invested in the PPP projects. Hence, these projects are expensive.
There is no problem of finance since the government supports the funding in large amounts.	The PPP projects are complicated, and inflexible.
The private sector organization in the PPP ensures higher level of efficiency, quality, and timely completion.	The difference in the functioning and work-culture of private and public sector can cause problems in the execution of project.

Not for profit social enterprises:

a) NGO

A private sector social enterprise that is not owned and controlled by the government and operates without the aim of profit maximization. NGOs focus on the humanitarian issues and work towards major social causes. Some examples of NGOs are **Greenpeace** (worldwide famous), **Goonj and Help age** (India), FICCI, etc.

Two types of NGO:

- *Operational NGO*- They focus on a development project.
- *Advocacy NGO*- These NGOs work for a particular cause by taking aggressive approaches such as lobbying, campaigning, demonstration.

गूंज..
GOONJ.. a voice, an effort

Founder of Goonj

Advantages of NGO	Disadvantages of NGO
NGOs work towards social cause and provide aid to various sections of the society.	There is no administrative body or central authority to govern/ regulate the activities of NGO.
The NGOs also receive tax exemption.	The registration of a non-governmental organization involves lot of paperwork.

b) Charities

The not-for-profit social enterprises that raise funds from individuals and organizations to voluntarily support for good causes by the means of donations.

E.g.- **World Wildlife Fund**, **Cancer research UK**, etc.

Major difference between charitable organizations and NGOs is the scope of work/operations. The NGOs work on a larger scale as compared to charitable organizations.

Pressure groups

Advocacy NGOs form a part of pressure groups. These are not for profit organizations that consist of individuals with common interest, that put demands on specific business organizations to act in a particular manner. These may include business groups, students' unions, religious organizations. Example- Greenpeace, **NSUI**, Brahmo Samaj, etc. They resort to measures such as lobbying, public relations, boycotting, etc. for the same.

Advantages of Charities	Disadvantages of charities
Being the non-profit organizations, charities are exempt from corporate tax.	Charites have to undergo various registration formalities before they start their operations.
The registered charities gain public trust and are therefore able to raise funds via donations easily.	They have limited sources of finance, the primary being the donations.
The charities work for social welfare and provide financial or in-kind aid to the needy sections of the society.	The absence of profitability factor leads to demotivation among the members, sometimes.