BUSINESS ORGANISATION

ECO-1

For

Bachelor of Commerce [B.Com.]

By

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Chapter-1

Basic Concepts and forms of Business Organisation

Q1. Define Business. What are the essential features and objectives of business? [Dec 2004, Q1(a)]

Ans. A **business** (also called a **firm** or an **enterprise**) is a legally recognized organization designed to provide goods and/or services to consumers. Businesses are predominant in capitalist economies, most being privately owned and formed to earn profit to increase the wealth of owners. The owners and operators of a business have as one of their main objectives *the receipt or generation of a financial return* in exchange for work and acceptance of risk. Notable exceptions include cooperative businesses and state-owned enterprises. Socialist systems involve either government agencies, public, or worker ownership of most sizable businesses.

The etymology of "business" relates to the state of being busy either as an individual or society as a whole, doing commercially viable and profitable work. The term "business" has at least three usages, depending on the scope — the singular usage (above) to mean a particular company or corporation, the generalized usage to refer to a particular market sector, such as "the music business" and compound forms such as agribusiness, or the broadest meaning to include all activity by the community of suppliers of goods and services. However, the exact definition of business, like much else in the philosophy of business, is a matter of debate.

Essential Features of Business: Following are the five broad features of business.

(a) Dealings in goods and services: Business deals with goods and services. The goods may be consumer goods such as sweets, bread, cloth, shoes, etc.: They may be producer's goods such as machinery, equipment, etc., which are used to produce further goods for consumption. Business also deals with services such as transport, warehousing, banking, insurance, etc., which are intangible and invisible goods.

(b) Production and/or exchange: You can call an economic activity a 'business' only when there is production or transfer or exchange or sale of goods or services for value. If goods are produced for self-consumption or presentation as gift, such activities shall not be treated as business. In a business activity, there must be two parties i.e., a buyer and a seller. Such activity should concern with the transfer of goods or exchange of goods between a buyer and a seller. The goods may be bartered or exchanged for money.

(c) Continuity and regularity in dealings: A single transaction shall not be treated as business. An activity is treated as business only whom it is undertaken continually or at least recurrently. For example, if a person sells his residential house, it is not considered as business. If he repeatedly buys houses and sells to others, such activity comes under business. But how frequently the transaction should occur depends on the nature of the activity. For example, a ship building company takes a long time to manufacture and sell a ship. At the same time, a vegetable vendor purchases vegetables from the market in the morning and sells out to his customers by evening. But both these activities are treated as business.

(d) Profit motive: Earning profit is the primary motive of business. This is not to undermine the importance of the element of service in business activity. In fact a business will flourish only when it is able to serve its customers to their satisfaction. Profits are essential to enable the business to survive, to grow, expand, and to get recognition.

(e) Element of risk: In every business, there is a possibility of incurring loss. This possibility of incurring loss is termed as risk. The element of risk exists due to a variety of factors which are outside the control of the business enterprise. There are two kinds of risks. (1) Risks whose probability can be calculated and can be insured. Losses due to fire, floods, theft, etc., are some examples. (2) Risks whose probability cannot be calculated and which cannot be insured against, e.g., changing technology, fall in demand, changing fashions, short supply of raw materials, etc. These risks are to be completely born by the enterprise.

Objectives of Business: According to Urwick, "profit can no more **be the objective of a business than eating is the objective of living".** Thus, serving the community is regarded as a important objective of business. **'The** objectives of business could be listed under three broad headings : (1) economic objectives, (2) social objectives, and (3) human objectives.

Economic Objectives : Some of the main economic objectives are :

(a) Earning of satisfactory profits.
(b) Exploring new markets and creation of more customers.
(c) Growth and expansion of business operations of the firm.
(d) Making innovations and improvements in goods and services so that customers get improved and more economic goods and services.

Social Objectives: Business, being a part of the society, has obligations towards the society I also. Some major social objectives are :

(a) Providing more and more employment opportunities to the people in the country.

(b) Supply of quality goods to the community.

(c) Providing goods at reasonable prices.

(d) Ensure fair returns to investors.

(e) Voidance of profiteering and unfair practices.

(f) Production of goods in accordance with national interests and priorities.

Human Objectives : Business activity is, generally, carried out through employees who are human beings. In fact, the efficiency and the success of the business enterprise depends on the motivation and ability of its employees. Therefore, business must also have some human objectives to safeguard the interests of its employees. Some of the major human objectives are :

(a) Fair deal to employees in terms of wages and incentives.

(b) Providing better working conditions and environment to the employees.

(c) Provide job satisfaction.

(d) Provide the employees more and more' promotional/growth opportunities.

Q2. Distinguish between profession, business and employment.
[June 2005, Q1(a)] [Dec 2003, Q1(a)]

Ans. Characteristics of Business, Profession and Employment :

Features	Business	Profession	Employment
Establishment	An individual or a group of individuals decides to start business. Legal formalities like registration etc. are to be fulfilled.	Acquire required qualification, training, etc. become the member of concerned professional body.	Enter into service contract with the employer.
Qualifications	Specific qualifications is not required.	Professional knowledge and training in the specific field is necessary	In some cases specific qualifications required and in some others cases not required
Investment	Capital is required, Actual amount depends on the nature of business	Some amount of capital required for equipment and establishment of office	Capital not required
Nature of work	Production and/or exchanges of goods and services.	Renders personalized services of a specialized nature to the clients	Performing the work assigned by the employer under the service contract
Motive	Mainly profit motive	Although fee is charged, service is the main motive	No specific motive. Mainly to earn livelihood
Reward	Profit	Professional fee	Wages or salary

Transferability of ownership interest	By following required legal formalities, business can be transferred to others.	Not possible to transfer	Not possible to transfer
Risk	There is risk of loss	Possibility of not getting enough fee to meet the expenditure on establishment	No risk, employee gets wage or salary regularly so long as the fame continues in operation

Q3. Define Industry. **[June 2008, Q1(a)]**

Ans. An **industry** (from Latin industrius, "diligent, industrious") is the manufacturing of a good or service within a category. Although industry is a broad term for any kind of economic production, in economics and urban planning industry is a synonym for the secondary sector, which is a type of economic activity involved in the manufacturing of raw materials into goods and products.

There are four key industrial economic sectors: the primary sector, largely raw material extraction industries such as mining and farming; the secondary sector, involving refining, construction, and manufacturing; the tertiary sector, which deals with services (such as law and medicine) and distribution of manufactured goods; and the quaternary sector, a relatively new type of knowledge industry focusing on technological research, design and development such as computer programming, and biochemistry. A fifth quinary sector has been proposed encompassing nonprofit activities. The economy is also broadly separated into public sector and private sector, with industry generally categorized as private.

Q4. What do you understand by commerce? Briefly explain the classification of commerce with suitable examples. **[Dec 2006, Q2]**

Ans. Commerce is a division of trade or production which deals with the exchange of goods and services from producer to final consumer. It comprises the trading of something of economic value such as goods, services, information or money between two or more entities. Commerce functions as the central mechanism which drives capitalism and certain other economic systems (but compare command economy, for example). **Commercialization** or **commercialisation** consists of the process of transforming something into a product, service or activity which one may then use in commerce.

The whole range of commerce activities can be classify into two categories:

(a) Trade-activities of purchase and sale.

(b) Aids to Trade- activities which facilitate the smooth and uninterrupted flow of goods.

Trade: A person who is engaged in trade is called 'trader' or 'middleman'. Various traders operate in between producers and consumers and remove the hindrance of person. We can classify trade into two broad categories: I) internal trade, and 2) external trade.

(1) Internal Trade: When the trade takes place within the boundaries of the country, you can call it 'internal trade'. It means that both buying and selling should take place within the country. Payment for the same is generally made in national currency. This internal trade is also termed as inland trade or national trade or home trade or domestic trade.

On the basis of the scale of operations, we can classify internal trade into: a) wholesale-trade, and b) retail trade.

(a) Wholesale Trade: Buying and selling in relatively larger quantities is called wholesale trade. A person who is involved in wholesale trade is called wholesaler.

(b) Retail Trade: This refers to buying and selling in relatively smaller quantities. A person engaged in retail trade is called a retailer.

(2) External Trade: This is also called 'foreign trade' or 'international trade'. When the trade takes place across the boundaries of a country, you can call such trade as external trade. In other words, external trade refers to the trade between nations. This trade could be in the form of exchange of one commodity for another or for money.

We can classify foreign trade into three categories: a) import trade, b) export trade, and c) re-export trade.

(a) Import Trade: when a country buys goods from another country, it is called import trade'. For example, India bought machinery from the USA. This is an import trade for India.

(b) Export Trade: When a country sells goods to another country, it is called 'Export Trade'. For example, India sells leather goods to USSR, and tea to USA in India such selling of goods shall be termed as 'export trade'.

(c) Re-export Trade: This is also called 'entrepot trade', Wheri the goods are imported from one country and the same are exported to another country, such trade is called 're-export trade'. Re-export is done by those countries which have ports that are conveniently situated to serve as distributing points for lieighbouring countries. Such countries import large quantities of goods and re-export the same to the neighbouring countries.

Aids to Trade: The whole range of activities coming under aids to trade may be classified into five categories: I) transportation, 2) warehousing, 3) insurance, 4) advertising, and 5) banking.

(1) Transportation: Generally, all the goods are not consumed at the same place where they are produced. Therefore, goods are to be moved from the place of production to the place where they are demanded. The activity which is concerned with such movement of goods is called ‘transportation’. Thus, transportation eliminates the hindrance of place and creates place utility to goods.

Transportation can be of three types :

(a) Land transportation - road, rail

(b) Air transportation-aeroplane

(c) Water transportation-boat, ship

(2) Warehousing: Goods may not be consumed immediately after production. Normally there will be time gap between production and consumption. This is the hindrance of time. Therefore, goods once produced should be preserved properly till they are consumed. Particularly, perishable goods like milk, meat, vegetables, flowers, etc., should be preserved very carefully. Otherwise, they get spoiled and become useless. For this reason warehousing is recognised as yet another aid to trade. Warehousing refers to preservation of goods to make them available as and when needed by consumers. Thus, warehousing eliminates the hindrance of time and provides time utility to goods.

(3) Insurance: The goods may be destroyed while in production process, or in transit due to accidents, or in storage due to fire or theft, etc. The businessmen would like to cover these risks. Insurance companies come to their rescue in this regard. They undertake to compensate the loss suffered due to such risks. For this purpose, the business has to take an ‘insurance policy’ and pay a certain amount regularly, called ‘premium’. Thus, insurance eliminates the hindrance of risk.

(4) Advertising: Exchange of goods is possible only when the consumers have the knowledge about the existence of a product. This is the hindrance of knowledge. This hindrance is eliminated through advertising. Through advertisement, producers communicate all information about their goods to the prospective consumers and create in them a strong desire to buy the product. Thus, advertising facilitates the flow of goods between producers and consumers by bringing the knowledge about the products to the consumers. Advertising is done through TV, radio, newspapers, magazines, hoardings, wallposters, etc.

(5) Banking : Banking facilitates the flaw of goods by removing the hindrance of finance and credit. Now-a-days we cannot think of business without banks. To start the business or to run it smoothly we require money. Banks supply money. A bank is an organisation whi’ch accepts deposits of money from the public, withdrawal on demand or otherwise, and lends the same to those who need it. Banks also provide many services required for **the**

business activity.

Q5. Write a short note on organization.

Ans. An **organization** (or **organisation** – see spelling differences) is a social arrangement which pursues collective goals, which controls its own performance, and which has a boundary separating it from its environment. The term is used in both daily and scientific English in multiple ways.

In the social sciences, organizations are studied by researchers from several disciplines, the most common of which are sociology, economics, political science, psychology, management, and organizational communication. The broad area is commonly referred to as organizational studies, organizational behavior or organization analysis. Therefore, a number of different theories and perspectives exist, some of which are compatible, and others that are competing.

(a) **Organization – process-related :** an entity is being (re-)organized (organization as task or action).

(b) **Organization – functional :** organization as a function of how entities like businesses or state authorities are used (organization as a permanent structure).

(c) **Organization – institutional :** an entity is an organization (organization as an actual purposeful structure within a social context)

Q6. What do you understand by sole trader organization? Discuss the merits and disadvantages of sole trader organization.

Ans. A sole trader business is a business owned by one person, although the organisation may employ more than one person. The sole trader's business will trade under the owner's name or a name chosen by the sole trader. To safeguard against legal proceedings the sole trader should ensure that they don't use a name registered to someone else.

A sole trader business is the simplest type of business organisation and the easiest to establish. There are no legal restrictions affecting the establishment of a sole trader business. A sole trader can keep all the profits. A sole trader does not need to keep accounts, but needs to ensure that they notify the Inland Revenue about their tax liability. To minimise tax liability many sole traders will employ accountants to draw up their final accounts and advise them about tax avoidance (not tax evasion).

Examples of sole trader businesses include small retailers, plumbers, builders, internet entrepreneurs, beauticians, market traders, grocers and butchers.

The main advantages of setting up as a sole trader are :

(a) **Total control** of the business by the owner.

(b) **Cheap and easy** to start up – few forms to fill in and to start trading the sole trader does not need to employ any specialist services, other than setting up a bank account and informing the tax offices.

(c) **Keep all the profit** – as the owner, all the profit belongs to the sole trader.

(d) **Business affairs are private** – competitors cannot see what you are earning, so will know less about how the business works and how it succeeds.

The reasons why sole traders are often successful are :

(a) Can offer **specialist services** to customers – e.g. appliance repair specialists.

(b) Can be **sensitive to the needs of customers** – since they are closer to the customer and will react more quickly, because they are the decision makers too.

(c) **Can cater for the needs of local people** – a small business in a local area can build up a following in the community due to trust – if people can see the owner they feel more comfortable than if the owner is in some far off town, not able to hear the views of the local community.

The main disadvantages of being a sole trader are :

(a) Unlimited liability

(b) Can be difficult to raise finance, because they are small, banks will not lend them large sums and they will not be able to use any other form of long-term finance unless they change their ownership status.

(c) Can be difficult to enjoy economies of scale, i.e. lower costs per unit due to higher levels of production. A sole trader, for instance, may not be able to buy in bulk and enjoy the same discounts as larger businesses.

(d) There is a problem of continuity if the sole trader retires or dies – what happens to the business next?

The reasons for being a sole trader are often a balance between business and personal costs and benefits. Many will prefer the satisfaction of running a business with little paper work against the risks, pressure and probably long working hours.

A sole trader is liable for any debts that the business incurs. This means that any money that the owner has put into the business could be lost, BUT IMPORTANTLY, if the business continues to incur further costs then the owner has to pay these as well. In some cases they may have sell some of their own possessions to pay creditors.

Such a risk often puts potential sole traders off setting up businesses, but also makes them consider the other forms of business structure.

Q7. Discuss about the partnership form of the organization.
[June 2008, Q3] [June 2005, Q2]

Ans. A **partnership** is a type of business entity in which **partners** (owners) share with each other the profits or losses of the business undertaking in which all have invested. Partnerships are often favored over corporations for taxation purposes, as the partnership structure does not generally incur a tax on profits before it is distributed to the partners (i.e. there is no dividend tax levied). However, depending on the partnership structure and the jurisdiction in which it operates, owners of a partnership may be exposed to greater personal liability than they would as shareholders of a corporation.

Advantages of Partnership :

(a) Easy to Form : The partnership, like the sole proprietorship, can be easily organized. There are no complicated legal formalities involved in the establishment of partnership business. The partners enter into a partnership agreement and start business.

(b) Favourable Credit Standing : The partnership enjoys a better credit rating in the eyes of creditors. As the liability of each partner in the organization is unlimited the financial institution can safely advance loans to the firms.

(c) Large Capital: In case of sole proprietorship, the capital is limited to the savings of one owner or his borrowing capacity. Partnership can bring more capital to the business by the joint efforts of the partners. The partnership is normally in strong position to raise capita and expand the business.

(d) Greater Management Ability: As there are many partners involved in the operation of a business, the firm can distribute the duties and responsibilities to each partner for which one is best qualified and suited. Division of labour and specialization, thus, can promote efficiency of the firm.

(e) Union of Business Ability: There is a bid age saying that two heads are better than one. In case of partner the partner mutually consults each other about the lay out, production procedure, marketing channels, etc. and as a result, a wise course of procedure results. **6. Profit Incentive:** The profits are shared by the partners as per agreement. They are encouraged to do more work to earn more profit. Higher the profits, higher will be the partners share.

(f) Advantages of Secrecy: The partners can keep the business secrets to themselves. The firm is not required by law to publish its profit and loss account and balance sheet.

(g) Retention of a Skilled Worker: If an employee in the partnership business is found to be a man of outstanding talent and ability, he with the mutual consultation of other partners can be given a status of a partner in the business.

(h) Brake on Hasty Decisions: As liability of partners is unlimited, the partners, therefore, tend to be careful in taking business decisions. They adopt sound practices in the conduct of business. There is a brake on hasty decisions.

(i) Special Protection to Minor: A death or lunacy of a partner may not cause dissolution of the partnership. His minor can be admitted only to the benefits of partners with the consent of other partners.

(j) Increase in The Spirit of Cooperation: The success of business depends upon mutual trust and cooperation of the partners. The partners are fully aware that a sight difference can cause the end of partnership. This increases in them the spirit of working together.

(k) Tax Advantage: The profits of a registered firm, after payment of super fax, are divided among the partners. They pay tax to the government on their shares of profit. Thus the partners of registered firm get the benefit of lower assessment.

(l) Ease of Dissolution : The partnership can also be legally dissolved much difficult by mutual consent of the partners or in accordance with a contract by the partners. There are no formal documents required to be drawn up as in the case of a joint stock company.

Disadvantages or Demerits of Partnership: The partnership form of organization suffers from certain disadvantages also. These in brief are as follows.

(a) Unlimited Liability of Partners: One of the basic defects of partnership is that the partners are personally and jointly responsible for all the debts of the firm. In case the business suffers losses and the business assets are not sufficient to satisfy the claimants on liquidation, the personal property of one or more than one partners can be sold under the Court order for the clearance of the debts of the business. The rich and wealthy persons, therefore, avoid to be enlisted in partnership because each individual partner in liable for the firm's debt.

(b) Limited Life of Firm: The duration of the partnership is always uncertain. I partner dies, injured, withdraws, sells his interest, or a new partner is admitted into the business, or their arises difference, the partnership may come to an end. There are every possibilities of the dissolution of the firm due to internal differences.

(c) Frozen Investment: It is very easy for a partner to invest money but it is most difficult to withdraw the from the business. A person who wishes to withdraw investment has to consult his partners, find a substitute with equal business ability. Unless the above conditions are fulfilled, the funds remain difficult to transfer and as such remain a frozen investment which creates lack of interest.

(d) Disputes Among The Partners : The partners should be like minded, have a common objective, be large hearted, have a cool temperament, should not unnecessarily cause friction and confusion among the partners. The choosing of partner is in fact like choosing a wife. Marry in haste and repent in leisure. In case of dispute among the partners, quick action should be taken by all the partners for the remedial measures.

(e) Possibility of Misuse of Resources: It is known to each and every partner that the resources of the firm are owned jointly. There can and does arise the misuse of resources by a partner/partners.

(f) Loss of Business Opportunities: In case of differences among the "partners, a delay may take place in decision-making. This can cause loss to the firm.

(g) Divided Control: In a partnership, the work of the business is divided among the partners according to their ability, choice and taste. Divided control - and responsibility sometimes creates confusion and delay in making decisions. The lack of efficiency on the part of one partner can upset the whole structure of the business and ultimately lead to dissolution of the firm.

(h) Lack of Public Confidence: Partnership form of organization may not enjoy public confidence due to lack of publicity and absence of regulations.

(i) Implied Authority: Implied authority is the authority vested in a partner to bind the firm with any of his acts done in connection with the business of the firms. In partnership form of organization, each partner binds other partners by his acts done on behalf of the firm: Thus the other partners may have to pay for the follies and dishonesty of a fellow partner.

(j) Conclusion: Partnership form of ownership is suitable where business is of medium size, the partners are of equal status, ability and resources.

Q8. What is Joint Hindu family firm? [June 2003, Q1(a)]

Ans. Joint Hindu Family Business is a form of organization in existence only in India. It is one of the oldest form of organizations and in existence only in some parts of the country. This form of organization has ownership in the hands of members of a Hindu undivided family.

The business is under the control of the head of the family known as the 'Karta'. The members of the family business are known as 'Co-partners'

Features :

- **(a) Organization Existence:** A joint Hindu family business exists due to the operation of Hindu law and not out of contract. The rights and liabilities of co-parceners are determined by the general rules applicable in the Hindu law.
- **(b) Membership:** A person born in the family gets an automatic membership of the business and legality is not affected by the minority of the member. There is no limit to the maximum number of members in this type of organization.
- **(c) Registration of Organization:** It is not necessary to get the business registered

(d) **Management:** The business is managed and controlled by the head or the 'Karta'. He has the power to obtain loans against the family property etc. The Co-partners do not have the power to raise loans or enter into contracts.

(e) **Unlimited Liability:** 'Karta' has unlimited liability and the co-parceners have limited liability to the extent of their individual investment in the family business.

Advantages:

(a) Ease of formation
(b) Continuous operations

Disadvantages:

(a) Applicable to Joint Hindu families
(b) Limited capital
(c) Limited managerial talents
(d) Unlimited liability of the Karta

Q9. What do you understand by the term 'Partnership Deed'?

Ans. Partnership Deed: A legal document formalizing the agreement and financial arrangements between the parties that make up a partnership.

Most partnerships write a Deed of Partnership when setting up. This legal document provides the rules of the business. A Deed of Partnership should include :

(a) Name of the firm.
(b) Nature of the business to be carried out.
(c) Name of the partners.
(d) The town and the place where business will be carried on.
(e) The amount of capital to be contributed between each partner.
(f) The profit and loss sharing ratio of each partner.
(g) Loans and advances by partners and the interest payable on them.
(h) The amount of drawings by each partner and the rate of interest allowed thereon.
(i) The rate of interest on capital.
(j) Duties, powers, and obligations of partners.
(k) Remuneration, if any, payable to the active partner.
(l) Maintenance of accounts and arrangement of audit.
(m) Settlement in the case of dissolution of partnership.
(n) The methods of evaluation of goodwill on admission or death or retirement of a partner.
(o) The method of revaluation of assets and liabilities on admission or death or retirement of a partner.
(p) The method of retirement of a partner, and the arrangement for the

payment of the dues of a retired or deceased partner.

(q) Arbitration in case of disputes among partners.

(r) Arrangements in case a partner becomes insolvent.

Registration of the firm : Under the Indian Partnership Act it is not compulsory to register the firm. But there are certain limitations for an unregistered firm. So, it is better to register it. Registration can be done at any time. To register the firm an application with all particulars about the firm and registration fee have to be sent to the Registrar of Firms.

Q10. Discuss about the company form of organization.

[June 2003, Q1]

Ans. Generally, a **company** is a form of business organization. The precise definition varies.

In the United States, a company is a corporation – or, less commonly, an association, partnership, or union – that carries on an industrial enterprise." Generally, a company may be a "corporation, partnership, association, joint-stock company, trust, fund, or organized group of persons, whether incorporated or not, and (in an official capacity) any receiver, trustee in bankruptcy, or similar official, or liquidating agent, for any of the foregoing."

Main Features: The features of the company form of organization are as follows:

(a) Incorporation: A company is an incorporated association. It comes into existence only after registration under the Companies Act.

(b) Artificial person: A company is regarded as an artificial person as it is created by law and can be effaced only by law. It has no body, no soul, no conscience, still it is in a position to exist. Like any other person it can own property, conduct a lawful business, enter into contracts with others, buy, sell and hold property, all under its own name and its own seal.

(c) Separate legal entity: A company has a distinct entity separate from its members. A shareholder of a company can enter into contract with the company and can sue the company and be sued by it. We know that in the case of partnership, every partner is an agent of the firm and also that of the other partners. But the shareholder is not the agent of the company or its shareholders. He can not bind them with his acts.

(d) Common seal: As the company is not a natural person, it can not sign the documents. It has a device in the form of common seal on which its name is engraved. This common seal is a substitute of its signatures. It is affixed on all important legal documents and contracts. It is used at the direction of the board of directors and two directors have to sign as witnesses wherever it is affixed on any document.

(e) Perpetual succession: A joint stock company has a continuous existence. Its life is not affected by the death, lunacy, insolvency or retirement of its shareholders or directors. Members may come and go, but the company continues its operations until it is legally dissolved. Thus, a company has perpetual succession irrespective of its membership. This feature provides stability to this form of organization.

(f) Separation of ownership and management: The shareholders of a company are widely scattered throughout the country. For the conduct of the business and its management, shareholders elect another set of persons known as directors. The right to manage the company affairs is vested in the directors who are elected representatives of the shareholders. Thus, ownership is separated from management.

(g) Number of members: In the case of a public limited company, the minimum number is seven and there is no maximum limit. In the case of a private limited company, minimum number is two and the maximum is fifty.

(h) Limited liability: The liability of the members of a company is normally limited by guarantee or by the shares. Members liability is limited to the amount of shares held. Members are not personally liable for the debts of the company. So, personal properties of the members are not liable to be attached for the payment of the company's debts.

For example, the face value of the share of a company is Rs. 10 which the member has already paid. At the time of winding up of the company, the member cannot be asked to pay any money. But if the member had paid only Rs. 7, he can at the most be asked to pay the balance of Rs. 3 (face value Rs. 10 minus money paid Rs. 7) and no more.

(i) Transferability of shares: The member of a public limited company enjoys a statutory right to sell his shares to others without the consent of other shareholders. But for transferring the shares he has to follow the procedure laid down in the Companies Act. However, there are restrictions for transferring shares in case of a private limited company.

(j) Rigidity of objects: The scope of the business of a company is limited. The type of business in which the company would participate is mentioned in the 'object clause' of its Memorandum of Association. The company cannot take up any new business without changing the object clause. To change the object clause, the company has to comply with the provisions of the Companies Act.

(k) Statutory regulations: A company is governed by the Companies Act and it has to follow various provisions of the Act. It has to submit a number of returns to the Government. Accounts of a company must be audited by a Chartered Accountant. Thus, the company form of organization has to comply with numerous and varied statutory requirements.

Merits and Limitations:

Merits :

(a) Large capital: Since company form of organizations are allowed to have a large number of shareholders, it is possible to raise capital in large amounts. Whenever new capital is required, it can issue shares and debentures. For this reason, only the company form of organization is best suited.

(b) Limited liability: The liability of shareholders, unless and otherwise stated, is limited to the face value of the shares held by them or guarantee given by them. Their private property is not attachable to recover the dues of the company. Thus, this form of organization is a great attraction to persons who are not willing to take risk as is inherent in sole proprietorship and partnership.

(c) Stability of existence: A company has a separate legal entity with perpetual succession. The corporation is not affected by lunacy or insolvency of a shareholder, director or officer. The continuity of the company is desirable in the interest of not only its members but also the society.

(d) Economies of scale: As companies operate on a large scale, they can take advantage of large scale buying, selling, production, etc. As a result of these economies of large scale operations, companies can provide goods to consumers at a cheaper price.

(e) Scope for expansion: As there is no limit to the maximum number of shareholders in a public limited company, expansion of business is easy by issuing new shares and debentures. Companies normally keep part of their profits as reserve and use them for expansion.

(f) Public confidence: Companies are subject to Government controls and regulations. Their accounts are audited by a chartered accountant and are to be published. This creates confidence in the public about the functioning of the company.

(g) Transferability of shares: The shares of the public limited company can be sold at any time in the stock exchange. Shareholders can sell their shares whenever they want. There is no need to take the consent of other shareholders. Thus, shareholders can convert their shares into cash at any time without much difficulty.

(h) Professional management: We know that the management of a company is in the hands of the directors who are elected by shareholders. Normally, experienced persons are elected as directors. We also know that day-to-day activities are managed by salaried managers. These managers are the experts in their respective fields. As companies have large scale operations and profits, attracting good professional managers is easy by paying attractive salaries. Thus, company form of organization gets the services of professionals on the Board of Directors and in various management positions.

(i) Tax benefits: Companies pay income tax at flat rates. There is no provision for slab system in the taxation of companies. As a result, companies pay lower taxes on higher incomes compared to other forms of organizations. Companies also get some tax concessions if they are established in backward areas.

(j) Risk diffused: As the membership is very large, the business risk is divided among the several members of the company. This is an advantage for small investors.

Limitations :

(a) Difficulty in formation: Promotion of a company is not as simple as proprietorship and partnerships. A number of persons known as promoters should be ready to associate themselves with it for getting a company incorporated. A lot of legal formalities are to be performed at the time of registration. Promotion of a company is expensive as well as complicated.

(b) Lack of secrecy: The management of companies is usually in the hands of many persons. Everything is discussed in the meetings of Board of Directors. Therefore, compared to sole trader and partnership concerns, maintaining business secrets is relatively difficult in a company form of organization.

(c) Delay in decision making: In company form of organization all important decisions are taken by either the Board of Directors or shareholders in their meetings. Hence, decision making process is time consuming. If a quick decision is needed it will be difficult to arrange meetings all of a sudden. So, more business opportunities may be lost because of delay in decision making.

(d) Neglect of minority interest: The representatives of the majority group of shareholders become the members in the Board of Directors. The shareholders who are in minority never get representation on the Board of Directors. As a consequence, the interests of the minority members may be neglected and oppressed at the hands of the majority group.

(e) Concentration of economic power: The company form of organization gives scope for concentration of economic power in a few hands. Some persons become directors in a number of companies and formulate policies to promote their personal interests. The shares of a number of other companies are purchased to create subsidiary companies. Establishment of subsidiary companies and interlocking of directorships have facilitated concentration of economic power in the hands of a few business houses.

(f) Lack of personal interest: In sole proprietorship and partnership firms business is managed by owners themselves. In company form of organization, day-to-day management is vested with the salaried executives who do not have any personal interest in the company. This may lead to reduced employee motivation and result in inefficiency.

(g) More government restrictions: The company is subject to many restrictions from which the proprietorship and partnerships are exempted. So, it has to spend considerable time and effort in complying with the various legal requirements.

(h) Fraudulent management: There is a possibility that some unscrupulous promoters may float a bogus company, issue shares and collect money. Later on, they can get away with the money by putting the company in liquidation. It is also possible that the directors and professional managers may misuse the company resources for their personal benefit and bring losses to the company.

Q11. Discuss briefly about the cooperative form of organization.
[Dec 2008, Q2] [Dec 2004, Q2]

Ans. A **cooperative** (also **co-operative** or **cooperative**; often referred to as a **co-op** or **coop**) is defined by the International Co-operative Alliance's Statement on the Co-operative Identity as an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise. It is a business organization owned and operated by a group of individuals for their mutual benefit. A cooperative may also be defined as a business owned and controlled equally by the people who use its services or who work at it. Cooperative enterprises are the focus of study in the field of cooperative economics.

Main Features: Following are the distinctive features of cooperative organizations:

(1) Voluntary association : As stated above, persons desirous of pursuing a common objective can form themselves into an association and leave the same as and when one likes. This has two important connotations:

(a) Any person can become a member irrespective of his caste, creed, religion, colour, sex, etc.

(b) The members come together to form themselves into an association without any coercion or intimidation.

(2) Autonomy and stability: Within the limits set by the constitution, the general law and its charter, a cooperative society is a self governing organization. It is self-sufficient, self-renewing and self-controlling within its jurisdiction. Like a company, a cooperative organization also enjoys a separate and independent entity distinct from that of its members. As such, it has a perpetual life and is not affected by the entry and exit of members.

(3) Democratic management : The management of cooperative organization vests in a managing committee elected by members on the basis of 'one member-one vote' irrespective of the number of shares held by any member. It is the general body of the members which lays down the broad framework of policy within which the managing committee has to function. Democracy is, thus, the keynote of the management of a cooperative society.

(4) Capital: The capital is procured from its members in the form of share capital. However, the share capital constitutes only a limited source of business finance. The major part is raised either by way of loan from the government and the apex cooperative institutions or by way of grants and assistance from the central or state governments.

(5) Government control: In India, all cooperative societies are registered under Cooperative Societies Act, 1919 or other State Cooperative Societies Act. Cooperative societies are subjected to detailed regulation under these Acts.

(6) Service motive: The primary objective of any cooperative society is to provide service to its members. As we know, in the case of the other three forms of organizations the primary objective is to earn profits.

(7) Limited return on capital: In cooperative system, profits are distributed among the shareholders for the capital they have contributed. But the rate of dividend paid to the shareholders is limited to 9% as per the Cooperative Societies Act.

(8) Distribution of surplus: In case of a partnership firm and a company, profits are distributed among the members in the ratio of the capital contributed by each of them. In case of cooperative societies, after giving a limited dividend to shareholders, the surplus profits are distributed in the form of bonus. This bonus is not in the proportion of the share capital, but in the proportion of the business they have done with the society. For example, in case of a consumer cooperative society, bonus is paid in the proportion of the purchases made by the members from the society. Similarly, in case of a producer's society, bonus is paid in the proportion of the goods delivered for sale to the society.

Merits and Limitations:

Merits:

(a) Easy formation: Formation of a cooperative society is easy as compared to the formation of a company. Cooperative society is a voluntary association and so it does not require long and complicated legal formalities at the time of formation. Any 10 adult persons can voluntarily from themselves into an association and get if registered with the Registrar of Cooperatives.

(b) Limited liability: Like company form of organization, liability of members is limited in cooperative societies also.

(c) Social services: Cooperatives foster fellow feeling among members and impart moral and educative values in their everyday life which are essential for better living.

(d) State assistance: Cooperatives have been adopted by the government as an instrument of economic policy. So, a number of grants, loans and financial assistance are offered by the government to these societies to make them function effectively.

(e) Open membership: The membership of cooperative societies is open to everybody. Nobody is debarred from joining on the basis of economic position, caste, colour or creed. There is no limit on the maximum number.

(f) Supply of goods at cheaper rates: The societies purchase goods directly from producers and sell them to the members at cheap rates. The middlemen are eliminated from the channel of distribution. The consumer cooperatives supply essential goods to the members at a time when there is scarcity of goods in the market. Even capital goods (like machinery, etc.) are procured directly from producers and are supplied to the members. So cooperative societies ensure regular supply of goods at cheaper rates.

Limitations:

(a) Lack of business acumen: Members normally do not have business experience. As a consequence, when they become the members of the Board of Directors the society is not conducted efficiently. Unlike companies, cooperatives cannot employ outside talents and trained personnel for improving the management competency. This is because such steps are incompatible with their avowed ends and limited means.

(b) Absence of mutual interest: A cooperative can only succeed when the members are imbued with a spirit of cooperation. Unfortunately, some influential members use the cooperative society as a source of their personal gains.

(c) Lack of interest: Sustained efforts over a period are the prerequisites for success in any business. But such a state of affairs does not exist in many cooperatives. Within a short period of its dramatic start, the cooperative becomes lifeless and inactive in its operation.

(d) Lack of coordination: It cannot be denied that internal dissensions and rivalries among the members sap much of its strength and vigour. The absence of coordinated and joint action is responsible for the collapse of many cooperative associations.

(e) Corruption: One of the most important drawbacks of a cooperative form of organization is the prevalence of corrupt practices in the management and functioning of the cooperative societies.

(f) Lack of secrecy: The affairs of cooperatives are generally exposed to the members and it becomes quite difficult for them to maintain secrecy in business affairs.

(g) Insufficient motivation : Since the rate of return on capital is low, the members do not feel involved in the affairs of the society.

Q12. What are the main requisites of an ideal form of business organization? [Dec 2003, Q2]

Ans. The requisites of an ideal form of organization are as follows :

(a) Ease of formation: An important factor for preferring a particular form of organization to another is the ease with which a business can be brought into existence. The comparative ease of difficulty in forming a particular form of organization mainly depends on three factors: (i) formation expenses by way of registration fee, stamp duty, fees of legal experts, charges involved in the drafting of documents, obtaining licenses, etc., (ii) legal formalities, and (iii) procedural delays, etc. Unless it is very essential, it is better to go for an organization which is easy to form.

(b) Scope of raising capital: The choice of organization mainly depends on the amount of capital required which is determined by the nature of business and the scale of operations. For example, if we want to open a retail shop in groceries, the amount of capital needed will not be much. But if we want to set up a sugar factory, we may require a large amount of capital. Ideal form of organization is one which provides scope for raising the amount of capital as and when required.

(c) Extent of liability: We know that the element of risk and uncertainty is prevalent in each business. In view of this, normally, the businessmen prefer limited liability. Obviously, limited liability is considered as an important feature of a good form of organization. However, a certain amount of risk is also found to be important to provide the needed spur for initiative, drive and involvement in business. Many times, the absence of such spur leads to weakness, inefficiency and even dishonesty on the part of management personnel.

(d) Flexibility of operations: The form of organization should be very flexible and adaptable to changing business conditions without much difficulty or complication. For example, if we want to expand our business, diversify or modernize the plant and equipment, the organization should be able to meet all requirements.

(e) Stability and continuity: Stability and long life of business is desirable from the point of view of owners, employees and customers. Employees always prefer a stable and continuous employment. If the business is stable, the owner should be able to formulate plans for the future and to make investments paying for a considerable length of time. From the customers' point of view also, regular supply of goods and services is expected to meet their needs. An ideal form of organization is one which provides reasonable amount of stability to the business.

(f) Effectiveness of management: As we know that the success of any business enterprise depends on the efficiency of management. Managerial efficiency depends on skills, motivation, flexibility, adaptability, etc. It is difficult for an individual to possess all these qualities.

(g) Extent of government control and regulations: If the governmental control and regulations are too many, the enterprise may have to divert a lot of time, money and energy for complying with legal formalities and instructions. In some cases there may be too much interference by the government officials in the day-to-day business of the firm. No doubt, the investors, creditors and customers trust the business enterprises whose activities are properly regulated by the government. But too much government interference is not favoured by the entrepreneurs because it mars their initiative and disrupts the working of their business.

(h) Business secrecy: In business, it is important to maintain business secrets without leaking them out to competitors. Therefore, a form of organization which enables retention of business secrets is preferred to the one wherein business secrets are difficult to preserve.

(i) Tax burden: Business taxes like sales tax, excise duty and customs duty are charged on certain products and services. Hence, such taxes affect all forms alike and they will not affect the choice. But the income tax liability is different from one form of organization to the other. Naturally, the form of organization which attracts the minimum amount of this tax liability is considered as an ideal form. From this point of view company form of organization is considered to be best because it enjoys a number of tax reliefs which are not available in case of other forms of organization.

(j) Ownership prerogatives: Some persons have a very strong desire to control the entire business activities themselves and place a great value upon their right of personal leadership. Some persons are desirous of sharing the responsibilities and risks of a business. Some people may want to own a part of the capital without a strong desire to control the affairs of the business. We can also find some persons who are not ready to bear the business risk. An ideal form of organization takes care of such prerogatives of the owners.

Q13. What is the criteria for the choice of organization?

[June 2006, Q2]

Ans. The decision regarding the choice of organization assumes importance at two stages of a business:

(a) At the time of staring a business.

(b) At the time of expansion.

Criteria at the Time of Starting a Business: Choice of a suitable form of business organization assumes great importance at the time of initiating or launching a new business enterprise because it is the form of organization which ultimately determines the power and responsibility of the entrepreneur. The choice is dependent on the following factors:

(a) Nature of business: Choice of a suitable form of organization is dependent on the nature of the proposed business. The organizational requirements are different for different types of business. For example, a big cement manufacturing activity and a retail cement shop cannot have the same form of organization. Similarly, the form of organization suitable for a textile mill is not suitable for a tailoring shop.

(b) Volume of business: The expected volume of business also influences the decision about the suitable form of organization. If the volume of business is small, we need small amount of capital and run less risk. In that case sole proprietorship may be quite suitable. But if the volume of business is large, we need more capital and run more risk which a single owner may find it difficult to cope with. So, partnership form or a company form would be considered more suitable.

(c) Area of operation: The area of operation of the business also influences the choice of form of organization. If the area is limited and confined to a particular locality, the suitable form of organization may be sole proprietorship. In case the area is widespread, the suitable form may be joint stock company.

(d) Desire for control: The extent of control and supervision will also determine the choice of organization. If it is desired to have a direct control over the business operations, a sole proprietorship or a partnership form of business should be adopted. In case if we feel that there is no need for direct control, the company form of organization is the best.

(e) Capital requirements: The form of organization will also depend on the extent of financial requirements of the business. A business which requires a small amount of capital can be organized on sole proprietorship or partnership basis. But if the financial requirements are huge, then the joint stock company form of organization may be preferred.

(f) Extent of risk and liability: We know business operations involve risk. If the promoters of a business enterprise are deterred by the risk involved, they will start the business on the basis of a limited liability. That means they can go for a company. In case they have capacity to bear the risk involved, it can be organized on sole proprietorship or partnership basis.

(g) Government regulations: As we know the governmental controls and regulations are more in company form and cooperative form of organizations compared to the remaining two forms. If we do not want too much government control and regulation, we should choose either sole proprietorship form or partnership form.

Criteria at the Time of Expansion: Growth is a normal phenomenon in business. When our business is successful, naturally, we may plan to expand it. The expansion programmes may have the following implications:

(i) Need for larger financial resources.

(ii) Need for internal reorganization and control.

(iii) Need for specialized services like communication, accounting, marketing, etc.

(iv) Increase in governmental controls and regulations.

(v) Increase in tax liability.

(vi) Increase in the problem of control and coordination.

In fact the nature of these problems will depend upon the nature of the existing business and type of expansion programme undertaken. To implement our expansion programme, we can either continue with the existing form of organization or adopt a new form of organization. Whatever alternative we choose, it must be able to meet all requirements of expansion. If our existing business is organized as a sole proprietor concern, we can think about employing a manager or taking a partner. In case it is a partnership firm, we may have to choose between increasing the number of partners or converting it into a private limited company. Similarly, if our existing business is in the form of a private company, we have the choice of converting it into a public limited company or not.

Q14. What do you understand by the term entrepreneurship? State the important characteristics of an entrepreneur. [June 2007, Q1(a)]

Ans. Entrepreneurship is the practice of starting new organizations or revitalizing mature organizations, particularly new businesses generally in response to identified opportunities. Entrepreneurship is often a difficult undertaking, as a vast majority of new businesses fail. Entrepreneurial activities are substantially different depending on the type of organization that is being started. Entrepreneurship ranges in scale from solo projects (even involving the entrepreneur only part-time) to major undertakings creating many job opportunities. Many "high-profile" entrepreneurial ventures seek venture capital or angel funding in order to raise capital to build the business. Angel investors generally seek returns of 20-30% and more extensive involvement in the business. Many kinds of organizations now exist to support would-be entrepreneurs, including specialized government agencies, business incubators, science parks, and some NGOs.

Characteristics of an entrepreneur : Entrepreneurs have many of the same character traits as leaders, similar to the early great man theories of leadership; however trait-based theories of entrepreneurship are increasingly being called into question. Entrepreneurs are often contrasted with managers and administrators who are said to be more methodical and less prone to risk-taking. Such person-centric models of entrepreneurship have shown to be of questionable validity, not least as many real-life entrepreneurs operate in teams rather than as single individuals. Still, a vast but now clearly dated literature studying the entrepreneurial personality found that certain traits seem to be associated with entrepreneurs :

(a) David McClelland (1961) described the entrepreneur as primarily motivated by an overwhelming need for achievement and strong urge to build.

(b) Collins and Moore (1970) studied 150 entrepreneurs and concluded that they are tough, pragmatic people driven by needs of independence and achievement. They seldom are willing to submit to authority.

(c) Bird (1992) sees entrepreneurs as mercurial, that is, prone to insights, brainstorms, deceptions, ingeniousness and resourcefulness. They are cunning, opportunistic, creative, and unsentimental.

(d) Cooper, Woo, & Dunkelberg (1988) argue that entrepreneurs exhibit extreme optimism in their decision-making processes. In a study of 2004 entrepreneurs they report that 81% indicate their personal odds of success as greater than 70% and a remarkable 33% seeing odds of success of 10 out of 10.

(e) Busenitz and Barney (1997) claim entrepreneurs are prone to overconfidence and over generalisations.

(f) Cole (1959) found there are four types of entrepreneur: the innovator, the calculating inventor, the over-optimistic promoter, and the organization builder. These types are not related to the personality but to the type of opportunity the entrepreneur faces.

Other characteristics include:

(a) The entrepreneur has an enthusiastic vision, the driving force of an enterprise.

(b) The entrepreneur's vision is usually supported by an interlocked collection of specific ideas not available to the marketplace.

(c) The overall blueprint to realize the vision is clear; however, details may be incomplete, flexible, and evolving.

(d) The entrepreneur promotes the vision with enthusiastic passion.

(e) With persistence and determination, the entrepreneur develops strategies to change the vision into reality.

(f) The entrepreneur takes the initial responsibility to cause a vision to become a success.

(g) Entrepreneurs take prudent risks. They assess costs, market/customer needs and persuade others to join and help.

(h) An entrepreneur is usually a positive thinker and a decision maker. An entrepreneur needs inspiration, motivation and sensibility.

Q15. What are the main functions of an entrepreneur?

[Dec 2008, Q1(b)

Ans. An entrepreneur frequently has to wear many hats. He has to perceive opportunity, plan, organize resources, and oversee production, marketing, and liaison with officials. Most importantly he has to innovate and bear risk. The main functions of an entrepreneur are as follows:

(1) Innovation: Innovation is one of the most important functions of an entrepreneur according to Schumpeter. An entrepreneur uses information, knowledge and intuition to come up with new products, new methods of reducing costs of a product, improvement in design or function of a product, discovering new markets or new ways of organization of industry. Through innovation, an entrepreneur converts a material into a resource or combines existing resources into new and more productive configurations. It is the creativity of an entrepreneur that results in invention [creation of new knowledge] and innovation [application of knowledge to create new products, services or processes.] Systematic innovation means monitoring the following for innovative opportunity :

- **(a)** The unexpected success or failure or any unexpected outside event, (e.g. when the IT bubble burst the ITES sector started growing.)
- **(b)** Innovation based on process need [e.g. plate based cameras, film based cameras, digital cameras]
- **(c)** Changes in industry and market structure [e.g. video cassette VCD, DVD, Blue ray disc]
- **(d)** Demographics changes (e.g. increasing number of working women and nuclear families in most metropolitan cities)
- **(e)** New knowledge (e.g. Pentium chip)

(2) Risk and uncertainty bearing: According to Hozelist an entrepreneur performs the function of risk and uncertainty bearing. Every decision pertaining to development of new products, adapting new technologies, opening up new markets involves risk. Decision-making in an environment of uncertainty requires anticipation of risk. Profit is said to be the reward for anticipating and taking such risks. However it is pertinent to mention that the entrepreneur is not a gambler, he only takes calculated risks. An entrepreneur develops the art of decision-making under conditions of uncertainty as a matter of survival.

(3) Organization building: An entrepreneur has to organize men, material and other resources. He has to perform the functions of planning, co-ordination and control. He has to use his leadership qualities to build a team, generate resources and solve problems. With his organizational skills an entrepreneur builds an enterprise from scratch, nurtures it and makes it grow. His vision sows the seeds for a sound and vibrant organization and synergies are built in the enterprise.

According to Kilby in a developing country even the imitator entrepreneurs are very important and the entrepreneurial role encompasses the following :

- **(a)** Perception of market opportunities
- **(b)** Gaining command over scarce resources
- **(c)** Purchasing inputs
- **(d)** Marketing the products
- **(e)** Dealing with bureaucrats
- **(f)** Managing human relations within the firm
- **(g)** Managing customer and supplier relations
- **(h)** Managing finance
- **(i)** Managing production
- **(j)** Acquiring and overseeing assembly of the factory
- **(k)** Industrial engineering
- **(l)** Upgrading process and product
- **(m)** Introducing new production techniques and products

Q16. List the types of promoters.

Ans. Types of Promoters: There are various types of promoters. They are classified as professional promoters, financial promoters, entrepreneurial promoters, institutional promoters and government.

- **(a)** **Institutional promoters:** There are some specialized institutions like Industrial Development Bank of India, National Industrial Development Corporation, etc., which are providing technical, managerial and financial assistance for the promotion of new enterprises. These institutions collaborate with other entrepreneurs to launch the enterprises.
- **(b)** **Entrepreneurial promoters:** These promoters conceive the idea of a new business unit, do the necessary preliminary work in setting up the business unit and ultimately control and manage the same. In India most promoters belong to this category.
- **(c)** **Government:** Since independence, Government of India has emerged as a big promoter of enterprises. It has promoted several enterprises in different fields such as ordnance factories, heavy electrical, shipping, iron and steel, fertilizers and pesticides, oil and natural gas, etc.
- **(d)** **Professional promoters:** These are specialists in forming new business enterprises. After promoting an enterprise they eventually handover the control and management to the shareholders of the company.
- **(e)** **Financial promoters:** These promoters float new enterprises during favourable conditions in securities market. They are people who have financial stability and are looking forward to new opportunities for

investment.

Q17. Discuss about the steps involved in the promotion of joint stock company.

Ans. A **joint stock company** (JSC) is a type of business entity: it is a type of corporation or partnership. Certificates of ownership (or stocks) are issued by the company in return for each contribution, and the shareholders are free to transfer their ownership interest at any time by selling their stockholding to others. In the United Kingdom, and elsewhere, there are two kinds of Joint Stock Company. The private company (sometimes called an "unlisted company") is one in which the shares are not offered for sale on the open market. The shares are usually only held by the directors and Company Secretary. The purpose of shareholding in such a company is to confer the financial protection of limited liability upon the owners.

In contrast, a public company (sometimes known as a "listed" company) offers its shares for sale upon the open market – they are "listed" upon the stock exchange. In Britain, they are usually distinguished by the letters "PLC" after their name. The public company can raise part of its capital by a share issue, but the directors have no control over the sale or purchase of its shares. Thus, a public company can be "taken over" by another through the act of purchasing a controlling interest in the shareholding.

Although not, strictly speaking, a joint stock company, a third kind of company is found in Britain. This is known as a guarantee company, and is only formed by societies and organisations for charitable purposes (e.g. sports clubs, hobby groups etc.), as there is no way that a profit can be distributed. No shares are issued, but a number of named directors "guarantee" a specified amount of debt for which they agree to be liable.

Now let us see what the promoters have to do for the registration of a company.

Registration of a Company: Registration of a company is also known as incorporation. A company is said to be incorporated when it receives the certificate of incorporation from the Registrar of Companies. The certificate of incorporation is a conclusive proof of the fact that a company bearing a specific name has been lawfully formed. The promoter has to take the following steps for obtaining the Certificate of Incorporation:

(1) Selecting a name for the company

(2) Preparation and printing the documents to be filled

(3) Filing the documents with the Registrar of Companies

Let us now take up these aspects one by one.

(1) Selecting a name: Every company to be registered should have a name by which it will be known for legal and business purposes. The promoters generally select a few names and ascertain from the Registrar's office whether these names are available. For this purpose an application on a prescribed form is submitted to the Company Law Administration, Government of India, through the Registrar of Companies for approval. The promoter can then adopt any name from the list of approved names. It is also necessary to include the words 'Limited' and 'Private Limited' in case of public limited company and private limited company respectively.

(2) Preparation and printing of documents: After the name of the company has been approved and adopted, the promoters have to get the following two documents prepared and printed:

(a) Memorandum of Association

(b) Articles of Association

Memorandum of Association: It is the most important document of a company as it lays down the constitution of the company and states the relationship of the company with the outside world. It is a public document and each person who deals with the company is supposed to know the provisions contained in the memorandum. The purpose of memorandum is to enable the shareholder, creditors and those who deal with the company to know what is its permitted range of activities. Although the company is a legal 'person' its capacity to do business, unlike that of a real person, is restricted. If a company is engaged in any trade or business which is outside the provisions of the Memorandum of Association, such acts are regarded *ultra vires* of the company and therefore, void and inoperative.

The Memorandum of Association contains the following particulars under different clauses :

(i) Name of the company

(ii) Name of the state in which the registered office is to be located.

(iii) Object clause –The nature of business activities which the company will undertake is to be stated in this clause.

(iv) A declaration that the liability of the members will be limited to the face value of shares subscribed.

(v) Capital clause – The total amount of capital with which the company is proposed to be registered and its divisions into different shares of a fixed amount are to be stated under this clause.

(vi) A declaration by signatories to the Memorandum that they are desirous of being formed into a company and agree to take the number of shares mentioned against their names.

The Articles of Association: It contains the rules and regulations relating to the management of its internal affairs. They define the rights, powers and duties of the management, the mode and form in which the business of the company is to be carried on and the manner in which changes in the internal regulations of the company may be made from time to time. Articles lay down the relations between the company and its members and between the members. A public company limited by shares may register its own Articles of Association or adopt Table A containing the model set of 99 articles given in Schedule I of the Companies Act. Other types of companies must prepare and file their own Articles of Association along with the memorandum at the time of incorporation. The Articles of Association must not contain anything contrary to the Companies Act, the public policy, the Memorandum of Association and the general law of the land.

(3) Filing of documents for registration: After preparing and printing the Memorandum of Association and Articles of Association, the promoters make an application to the Registrar of Companies and file the following documents:

(i) A copy of the Memorandum of Association

(ii) A copy of the Articles of Association

(iii) A list of persons who have agreed to become director of the company with their names, addresses, age and occupations. In case a separate list of directors is not filed, signatories to the Memorandum of Association will be deemed to be the directors.

(iv) Written consent of the directors to act in that capacity, duly signed by each director, along with a written undertaking to take the prescribed qualification shares, if any. A company without share capital and a private company need not file this document.

(v) A statutory declaration stating that all the legal requirements with respect to incorporation have been duly compiled with. This declaration should be signed by an Advocate of a High Court or of the Supreme Court or by a practicing chartered accountant or by a person named as director, manager or secretary of the company.

(vi) Notice of the registered office of the company. However, this notice may be filed within 30 days of incorporation.

Along with the above documents, the Memorandum of Association and the Articles of Association must bear stamp duty as per the Indian Stamps Act. The promoters have also arranged payment of registration fees and filing fees at the time of submitting the application. If the Registrar upon scrutiny of the documents finds them to be in order, he issues the Certificate of Incorporation in favour of the company. The company becomes a separate entity in law when it gets the Certificate.

Commencement of Business : A private limited company can commence business activities as soon as it is registered. The promoters of such a company raise the amount of capital necessary from their friends and relatives either against shares issued or in the form of loan. The general public cannot be invited to contribute to the capital.

For a public limited company, however, business activities cannot be started immediately after registration. It has to obtain a Certificate of Commencement of Business from the Registrar of Companies for which a number of additional steps have to be taken by the promoters. They are as follows:

(a) Preparation and registration of Prospectus or a Statement in lieu of Prospectus: After the company has been incorporated, it is necessary for the directors to raise necessary capital for the company. Generally, shares of fixed amount are decided to be issued to the public to raise the amount of capital required. The document which is prepared to invite the public to subscribe to the shares of the company is known as Prospectus. In fact, the prospectus includes all such information about the company which may be of interest to the people who are likely to subscribe to the capital. The content of the prospectus have been specified in the Companies Act, so that the promoters may not suppress anything or mislead the public. A copy of the prospectus is required to be filed with the Registrar for registration before it is issued to the public. A private limited company does not have to issue a prospectus to raise its capital since it is not permitted under law to invite the public to subscribe to its shares. However, it is not compulsory even for a public limited company to issue prospectus unless it decides to approach the public for raising its capital. If the promoters decide not to approach the public for raising the necessary capital but to arrange subscription of capital by their friends or relatives or through underwriters, it is not necessary for them to issue a prospectus. In that case, a **Statement in lieu of Prospectus** must be filed with the Registrar. The contents of such a statement are virtually the same as those of a Prospectus. The Statement must be signed by all the directors of the company and filed with the Registrar.

(b) Subscription and Allotment of Shares: If public offer for sale of shares and debentures exceeds Rs. 1 crore, the company must obtain the permission of the Controller of Capital Issues, New Delhi. After obtaining such permission and the registration of prospectus with the Registrar, the company can invite public to subscribe to its shares. The companies usually appoint brokers through whom they approach the public for subscription. The brokers issue prospectus and application forms to the prospective investors. The company also appoints some banks who receive the applications from the public along with the application money and credit the amount to company's account specially opened for the purpose. After the issue is closed, the Board of Directors decide the basis of allotment in consultation with the stock exchange authorities and pass a formal resolution for allotment. On the basis of the resolution the Secretary of the company issues letters of allotment to the subscribers. If the subscription exceeds the amount of capital to be raised, the excess is refunded to the subscribers involved. After the allotment exercise is over, the Secretary submits a Return of Allotment to the Registrar of Companies.

One of the important conditions to be fulfilled by a public limited company before it can apply for the Certificate of Commencement of Business is that it must have received share applications for the **minimum subscription** as indicated in the prospectus. Minimum subscription is defined as the minimum amount which in the opinion of the directors (or the signatories of the Memorandum), must be raised by issue of shares to meet the following expenses :

- **(i)** purchase price of any property bought or to be bought which is to be paid out of the proceeds of the share issue;
- **(ii)** preliminary expenses;
- **(iii)** repayment of money borrowed in respect of the above matters;
- **(iv)** working capital required; and
- **(v)** any other payment that may be specified.

If the amount of capital subscribed by the public is less than the minimum subscription or the company could not obtain minimum subscription within 120 days of the issue of prospectus, all money received from the applicants have to be refunded and no allotment can be done.

(c) Declaration of Compliance: When all the formalities in respect of the public issue have been completed, the company will have to file a statement with the following declarations with the Registrar:

- **(i)** That the shares payable in cash have been allotted up to the amount of minimum subscription as stated in the prospectus.
- **(ii)** That every director has paid in cash the application and allotment money on his shares in the same proportion as others.
- **(iii)** That no money is liable to become refundable to the applicants by reason of failure to apply for permission for shares and debentures to be dealt in on any recognized stock exchange.
- **(iv)** The statutory declaration by the Secretary or one of the directors that the above requirements have been complied with.

A company which has not issued a prospectus can submit the declaration immediately after the statement in lieu of prospectus has been filed and other conditions have been fulfilled. A private limited company is not required to submit any declaration, as it is permitted to commence business immediately after incorporation of the company. The Registrar of companies will scrutinize all these documents and if satisfied, he shall issue a ‘Certificate of Commencement of Business’. After this, the company is entitled to commence business and borrow money from the date of issue of the certificate.

Chapter-2

Financing of Business

Q1. Discuss the types of financial needs.

Ans. There are two ways of classifying the financial needs of the business:

(i) On the basis of the extent of permanence, we can classify the financial needs into:

(a) fixed capital, and

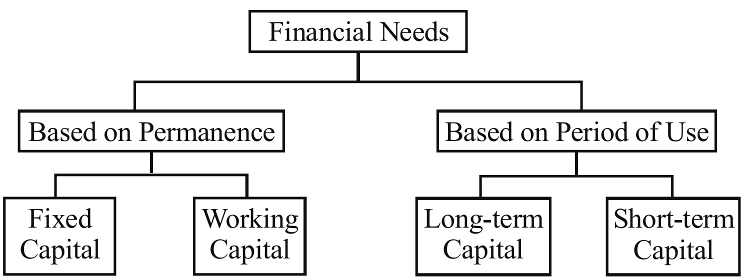
(b) working capital

(ii) On the basis of the period of use, we can classify the financial needs into :

(a) long-term capital, and

(b) short-term capital

Classification of Financial Needs



Fixed Capital and Working Capital :

Fixed Capital: In every business concern money has to be invested in some fixed or durable assets like land, buildings, machinery, equipment, furniture, etc. These assets are required for permanent use, that is, for a long period of time. Funds required to purchase these assets is known as fixed capital or long-term capital. The nature and size of the business generally determines the amount of fixed capital needed. Manufacturing activities, particularly those engaged in heavy engineering, electrical, transport, shipping and ship building, electric supply, iron and steel manufacture, automobiles, etc. require large investments in plant and machinery, equipment, factory buildings, warehouses, etc. On the other hand, trading concerns need relatively lesser investment in fixed assets.

Investment in fixed assets involves a commitment for a longer period of time. These fixed assets continue to generate income and profits over an extended period of time. Moreover, funds which are once invested in fixed assets cannot be withdrawn and put to some other use.

Working Capital: In business we require finance for purchase of raw material, payment of wages and salaries, rent, fuel, electricity and water, repairs and maintenance of machinery, advertising, etc. Requirements of finance for these purposes arise at short intervals. In course of business activities, it is also necessary to hold stocks of materials, spare parts and finished goods. This involves investment in short-term assets or current assets in the form of stocks of raw materials, spare parts, stores, finished goods, etc. Besides, sale of goods on credit leads to the holding of debtors balances and bills receivable, which may also be regarded as current assets.

Money invested in current assets like stock of raw materials, finished goods, etc. and book debts (that is debtors balances as well as bills receivable) is known as **Working Capital**. It is sometimes known as **Circulating Capital or Revolving Capital**. That is because funds invested in current assets are continuously recovered through realization of cash and again reinvested in current assets. The amount keeps on circulating or revolving from cash to current assets and back again to cash. Although this takes place at short intervals, the amount is needed again and again. Hence part of the funds required for this purpose is of a permanent nature. It is known as the ‘fixed or permanent’ part of the working capital. The permanent part of working capital should accordingly be regarded as long term capital. The other part of working capital may vary due to the rise or fall in the volume of business. Hence it is known as the ‘fluctuating’ or ‘variable’ part of the working capital. Therefore, strictly speaking, only the fluctuating part of the working capital is regarded as short-term capital, the funds required are for less than a year. The amount of working capital required depends mainly on the nature of the business, the time required for completing the manufacturing process and the terms on which materials are purchased and goods are sold. For instance, trading companies require more working capital than manufacturing companies. This is because the trading business requires large quantities of goods to be held in stock and also carry large debtors’ balances. Construction companies also require relatively larger amounts of working capital than manufacturing concerns. In both these types of business, the value of current assets is about 80% to 90% of the value of total assets. The investment in current assets is relatively smaller in the case of hotels and restaurants because they mostly have cash sales and only small amounts of debtors balances.

Working capital requirements vary among manufacturing industries because of differences in the time involved in the production process i.e., time that passes between the purchase of raw materials and the production of finished goods. Longer the processing time, the more is the amount of working capital required. For example, heavy engineering industry needs relatively more working capital than a rice mill or a cotton spinning mill or a steel rolling mill.

Another factor that determines the amount of working capital relates to the terms of credit allowed to customers. For instance, a company may allow only 15 days' credit, while another may allow 90 days' credit. One may extend credit facilities liberally to all customers, while another in the same business may grant credit only to selected reliable customers. The amount of working capital required will naturally be more if the credit period is longer and credit facilities are extended to all customers. In both these cases, there will be larger debtors' balance which will demand more working capital. On the other hand, if supplies of materials are available on favourable terms of credit (i.e., payment can be made at longer intervals), working capital needs will be correspondingly smaller.

Long-term Capital and Short-term Capital: As stated earlier fixed assets should be financed with permanent long-term capital. This is mainly because fixed assets are meant for use over a fairly long period of time, generally for five years or more. Long term capital is also required to finance the permanent part of the working capital. On the other hand, to finance current assets and meeting day-to-day expenses, capital is needed generally for a short period i.e., less than a year. This is because stocks of materials and finished goods are normally used for as sold within a year and dues from customers are usually realized within three to six months. The main difference between long-term capital and short-term capital is that the former is required for a longer period, (five years or more) while the latter is required for a short-time period (less than a year). Besides these capital needs, business concerns often require funds for a period of 2 to 5 years known as **medium-term capital**. Medium-term capital is required for certain activities like renovation of building, modernization of machinery, heavy expenditure on advertising, etc.

Q2. What is Capital Structure? [Dec 2006, Q3] [Dec 2004, Q3]

Ans. In finance, **capital structure** refers to the way a corporation finances its assets through some combination of equity, debt, or hybrid securities. A firm's capital structure is then the composition or 'structure' of its liabilities. For example, a firm that sells \$20 billion in equity and \$80 billion in debt is said to be 20% equity-financed and 80% debt-financed. The firm's ratio of debt to total financing, 80% in this example, is referred to as the firm's leverage. In reality, capital structure may be highly complex and include tens of sources.

The Modigliani-Miller theorem, proposed by Franco Modigliani and Merton Miller, forms the basis for modern thinking on capital structure, though it is generally viewed as a purely theoretical result since it assumes away many important factors in the capital structure decision. The theorem states that, in a perfect market, the value of a firm is irrelevant to how that firm is financed. This result provides the base with which to examine real world reasons why capital structure *is* relevant, that is, a company's value is affected by the capital structure it employs. These other reasons include bankruptcy costs, agency costs, taxes, information asymmetry, to name some. This analysis can then be extended to look at whether there is in fact an optimal capital structure: the one which maximizes the value of the firm.

Q3. What factors should management take into account while deciding on a capital structure? [Dec 2004, Q3]

Ans. Factors Determining the Capital Structure:

(a) Nature of the business: If a company is engaged in business activities in which sales are subject to wide fluctuations, it is desirable to have a smaller proportion of borrowed funds. Companies manufacturing televisions, refrigerators, machine tools and capital goods are normally subject to fluctuations in sales from time to time. If these companies have high debt ratios, they run the risk of facing financial distress during lean business due to their inability to discharge the fixed obligations. On the other hand, companies dealing in essential consumer goods of daily use or products having inelastic generally have stable earnings and thus may depend to a greater extent on borrowed capital.

Competitiveness among companies is also another aspect of business which may affect the level of earnings. For instance in the ready-made garment industry, competition among the firms is based on styles which are subject to frequent changes and mostly unpredictable. Hence, these firms rely less on borrowed capital and more on equity finance.

(b) Characteristics of the company: The size of a company as well as its credit standing also determines the extent to which equity or debt capital should be raised. Small firms have to depend more on owners' funds as it is difficult for them to raise long-term loans. This is because investors consider lending to small firms to be more risky. In contrast, large companies must make use of different sources of raising funds as no single source can meet their total financial requirements. Normally investors prefer to lend money to large companies as they believe that their money is safe and the risk is less with big business firms. Similarly, firms which enjoy high credit standing among investors and lenders are in a better position to raise long-term finance from different sources.

(c) Management control: Promoters who had major share holding and control the management of the company take into account the probable effect of raising funds through the issue of equity shares. Equity shareholders having voting rights can influence the policy decisions of the company or the selection of directors. But the persons who give loans do not have any right to elect directors or to participate in the management of the company. Hence the existing management group, in order to retain their control over management, prefer to raise additional finance through the issue of debentures and preference shares.

(d) Cost of finance: Since interest paid on borrowings is chargeable to profits before tax calculation, the cost of debt financing is inevitably lower than the expected rate of earnings (i.e. profitability) on equity capital. Hence, it is always beneficial to raise part of the total financial requirement through long-term loans. With lower cost of debt financing, the overall (average) cost of financing is reduced and the return on equity capital is higher. This is one of the important determinants of the capital structure.

(e) Effect of debt financing on the earnings per equity share: We have already explained how the rate of return on equity share capital increases if borrowed capital is used. The effect of debt on the rate of return on equity (or earning per share) is known as **'trading on equity' or 'leverage effect'**. Thus in business ventures with assured prospect of rising income, there is greater emphasis on debt capital in the capital structure.

(f) Expected earning in relation to interest charges: Another factor determining debt-equity ratio is the estimated coverage of interest by profits. If the average earnings of the company are expected to be three to four times the amount of interest payable on borrowed capital, it may be considered safe to raise long-term loans rather than equity capital. Three to four times coverage of interest by earnings is regarded as a reasonable assurance that interest payment would be possible even if profits decline substantially.

(g) Availability of cash (cash flow): The ability of a business to discharge its fixed obligations depends essentially on the availability of liquid cash. Profits earned may be adequate to cover the fixed charges arising out of debt, but the firm may not have sufficient cash to pay as the income gets continually invested in the form of more inventory, book debts or even purchase of equipment, particularly, if it is a growing concern. Hence, besides profitability, it is necessary to estimate the cash flows before deciding on the proportion of debt in the capital structure.

(h) Flexibility of capital structure: The capital structure decision is usually made by management keeping in view their ability to adjust the sources of funds. The scope of changing the capital structure in future happens to be a basic consideration. For instance, in case additional funds are needed, a firm which is already financed with heavy debt may be forced to issue equity shares with a higher cost of finance involved. Or, again if funds raised are to be refunded on account of declining business, a firm may be unable to do so if it earlier relied heavily on equity capital. Indeed, to preserve operating flexibility, it is desirable that every firm should have unused debt raising capacity for future use. On the other hand, there should be a judicious mix of debt and equity capital so that refund of debt is possible when necessary.

Q4. What do you understand by the term 'capital rising'? Briefly discuss the methods of raising capital. [June 2008, Q4)]

Ans. Capital Raising: When a business wants to expand or commercialize a new product or service, there comes a time when the business needs to raise capital. The Capital Raising Program aims to help clarify your business growth plans and prepare your business to raise capital. The available options under the program include:

Step 1 – Capital Raising Self-Assessment Tool: The first step is to make sure you have information on the options for raising capital. The attached Capital Raising Diagnostic is a self-assessment tool to help identify how ready your business is to raise capital. After considering this information, you may want to seek advice from the Department of State and Regional Development (DSRD). A DSRD officer can make a referral to either the Capital Raising Program or another service.

Step 2 - Funding Business Growth Workshops: These free workshops are conducted as required in different NSW regions. Participant numbers are limited and preference will be given to businesses who can demonstrate their growth potential. Contact DSRD to find out if a workshop is being held near you.

Step 3 – Business Diagnostic or Position Analysis: Eligible businesses can apply for a two hour Business Diagnostic session with guidance from an experienced consultant using the attached diagnostic tool. A Position Analysis is a more detailed and tailored assessment of business growth potential, capital requirements, capital structure to finance growth and business improvements that need to be implemented to raise capital. The cost of both these options can be subsidized by DSRD.

Step 4 – Equity Raising Preparation: Assistance can include attending an "Accessing Equity Capital" workshop, tailored assistance to implement business improvements to increase capability to raise equity finance, and help with preparing a pitch and investment matching.

Methods of Raising Capital: For a sole proprietor, there are limited opportunities for raising funds. He can finance his business by any of the following means:

(a) Investment of own savings
(b) Raising loans from friends and relatives
(c) Arranging advances from commercial banks
(d) Borrowing from finance companies

The same methods of financing are available to partnership firms also. In both these forms of business organizations, long-term capital is generally provided by the owners, i.e., sole proprietor or the partners.

Fixed capital can be raised by way of loans from friends and relatives on the personal security of owners. Generally short-term working capital needs are met partly by trade creditors (suppliers of materials and goods) and loans from finance companies. Another method of securing both long and short-term finance is the reinvestment of profits earned from time to time.

In the case of companies, there are a number of methods of raising finance. To raise long-term and medium-term capital, companies have the following options :

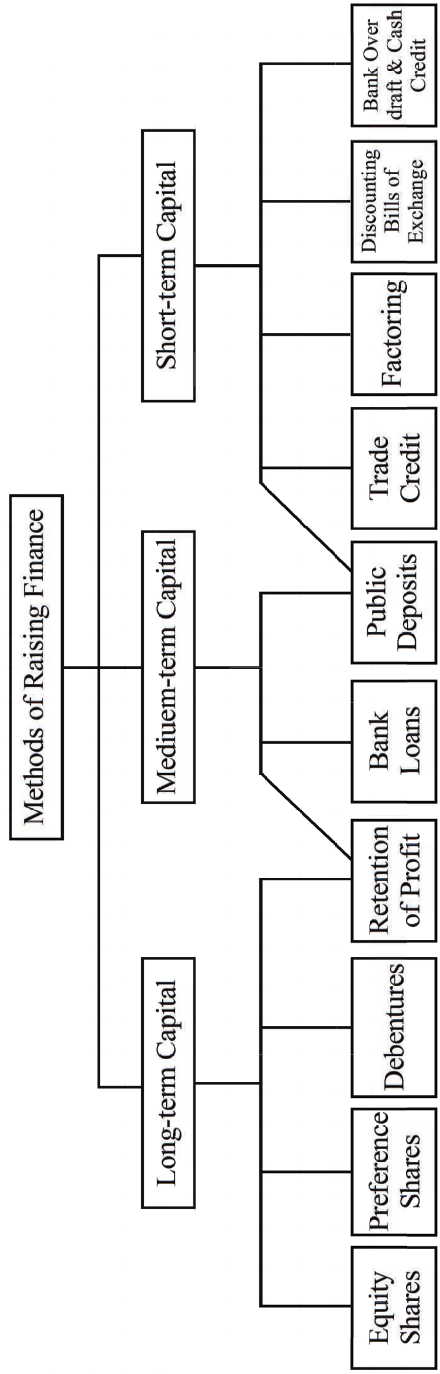
(a) Issue of shares
(b) Issue of debentures
(c) Loans from financial institutions
(d) Loans from commercial banks
(e) Public deposits
(f) Retention of profits

The following methods may be used to finance short-term capital :

(a) Trade credit
(b) Factoring
(c) Discounting bills of exchange
(d) Bank overdraft and cash credit
(e) Public deposits

Look at following Figure for various methods adopted by companies for raising finance.

Methods of Raising Finance by Companies



Q5. Distinguish between issue of shares and issue of debentures.

Ans. Issue of Shares: Issue of shares is the most important method of raising long-term capital for companies. There are two types of shares: (i) equity shares and (ii) preference shares. In the case of shares, the liability of shareholders is limited to the face value of shares and also they are easily transferable. A private company cannot invite the general public to subscribe for its share capital. Private companies can issue shares to a limited number of persons not exceeding fifty. Also shares of private companies are not freely transferable. But for public limited companies there are no such restrictions.

(a) Equity shares: There are several advantages of issuing equity shares to raise ownership capital. The rate of dividend on these shares depends on profits available and the discretion of directors. There is, therefore, no fixed burden on the company. The shareholders expect high rates of dividend in profitable years. But they also bear the risk associated with uncertainty of earnings of the company. Thus, risk capital is available by issuing these shares. Further, the amount raised by issue of equity shares can be used permanently. It is not required to be paid back so long as the company exists. Moreover, equity shares do not require mortgaging of the company's assets. Additional funds can be raised as loan on the security of assets.

However, excessive issue of equity shares may create problems for the promoters who may like to control the management of the company. Each equity share carriers one vote for the holder. So holders of equity shares may form groups and vote against the existing directors of the company. This may not be always in the best interest of the company as a whole. Secondly exclusive dependence on equity share capital may not permit the company to take advantage of trading on equity. Besides, once equity shares are issued the amount become a permanent capital which at times may be more than what the company can use profitably. In that case, there is no way of reducing it unless detailed legal formalities are complied with. Also reduction of share capital damages the image of the company.

(b) Preference shares: Issue of preference shares is another method of raising long-term capital. It has certain merits. Dividend is payable on preference shares at a fixed rate and is payable only if there are profits. Hence, there is no compulsory burden on the company's finances. Secondly, preference shareholders do not have voting right. So they cannot take part in the management of the company and thus are not a threat to the promoters. Another advantage of preference shares is that the company can declare higher rates of dividend for equity shareholders in good years because the rate of preference dividend is fixed. Besides, permanent use of preference share capital is also not essential. A company may issue redeemable preference shares and have the flexibility of paying off the amount if necessary and replace it by some other type of capital.

Some investors subscribe to preference shares because of preferential rights as to the payment of dividend and the return of capital. But others do not prefer it due to the fixed return as well as some risk of non-payment of dividend. Also they do not derive any benefit by way of rise in market price of the shares as is the case with equity shares.

Issue of Debentures : Companies generally have powers to borrow and raise loans by issuing debentures as securities of specified face value. The rate of interest payable on debentures is fixed at the time of issue and they are recovered by a charge on the property or assets of the company, which provide the necessary security for payment. Debentures are mostly issued to finance the long-term requirements of business. There are certain advantages of issuing debentures.

(i) Because of the fixed interest on debentures, companies with stable income can secure higher returns on equity capital by trading on equity.

(ii) The rate of interest is usually lower than the expected rate of return on share capital. This is because debenture holders do not bear any risk.

(iii) Debentures do not carry any voting right. Hence management by promoters or existing directors remains unaffected.

However, if the earnings of the company are uncertain or unpredictable, issue of debentures may pose serious problems for the company due to the fixed obligation to pay interest and repay the principal. The company is liable to pay interest even if there is no profit. If there is default in payment of interest or repayment of the principal, assets can be attached by order of the court. Trading companies which generally do not have large fixed assets, cannot provide adequate security for issue of debentures. Even for manufacturing companies the capacity to raise loans is limited by the value of their properties and assets.

Q6. What do you understand by Public deposits?

Ans. Companies often find it convenient and necessary to raise funds by inviting their shareholders, employees and the general public to deposit their savings with the company. The Companies Act permits such deposits to be received for a period up to 3 years at a time. Thus, public deposits can be raised by companies to meet their short-term and medium-term financial needs. It is a simple method of raising finance for which the company has only to advertise in the newspapers giving particulars about its financial position as prescribed by the Companies Act. The deposits are not required to be covered by mortgaging assets or by other securities. Moreover deposits can be invited by offering a higher rate of interest than the interest on bank deposits.

But companies are not permitted to raise unlimited amounts of fund through public deposits. The aggregate of all outstanding deposits cannot exceed 25% of the paid up capital and free reserves of the company. Interest to be allowed on deposits must also be in accordance with the rate fixed by the Government. Further, it is laid down in the Companies Act that at the beginning of each year, the company must deposit in a bank at least 10% of the deposits maturing during that year or invest an equivalent amount in Government securities for repayment of deposits. Besides, the company has to file a return or statement every year with the Registrar of Companies giving all information relating to the deposits.

However, small scale industries (i.e. manufacturing companies with investment in plant and machinery not exceeding Rs. 35 lakhs) are exempted from the restrictions as to the maximum limit of deposits if the following conditions are satisfied:

(i) The amount of deposit does not exceed Rs. 8 lakhs or the amount of paid up capital whichever is less.

(ii) The paid up capital does not exceed Rs. 12 lakhs.

(iii) The number of depositors is not more than 50%.

(iv) There is no invitation to the public for deposits.

Q7. Taking into account sources of long term finance write a short note on followings :

(1) Capital Market **(2) Leasing Companies**

(3) Foreign Sources **(4) Retained profit** **[Dec 2003, Q1(b)]**

Ans. (1) Capital Market : The **capital market** is the market for securities, where companies and governments can raise longterm funds. It is a market in which money is lent for periods longer than a year. The capital market includes the stock market and the bond market. Financial regulators, such as the U.S. Securities and Exchange Commission, oversee the capital markets in their designated countries to ensure that investors are protected against fraud.

The capital markets consist of the primary market and the secondary market. The primary markets is where new stock and bonds issues are sold (underwriting) to investors. The secondary markets are where existing securities are sold and bought from one investor or speculator to another, usually on an exchange (e.g. New York Stock Exchange, Delhi Stock Exchange.)

(2) Leasing Companies : Manufacturing companies can secure long-term funds from leasing companies. For this purpose a lease agreement is made whereby plant and machinery and fixed assets may be purchased by the leasing company and allowed to be used by the manufacturing concern for a specified period on payment of an annual rental. At the end of the period the manufacturing company (lessee) may have the option of purchasing the asset at a reduced price. The ownership of the asset remains with the leasing company (lessor) during the lease period. To meet its financial requirements, a manufacturing company may also sell its existing fixed assets to a leasing company at the current market price on the condition that the leasing company would lease the assets back to the seller for a specified period. Such an arrangement is known as **'sale and lease back'**. The manufacturing company in this case gets the fund immediately without having to part with the physical possession of the assets. It continues to use the assets on payment of periodical rent for the lease. In any type of lease agreement, the lease rent includes an element of interest besides expenses and profits of the leasing company. Actually, the leasing company makes an investment of its own funds and must earn an income as a return on its investment through the lease rents.

(3) Foreign Sources: Funds can also be collected from foreign sources which usually consist of: (i) foreign collaborator, (ii) international financial institutions, and (iii) non-resident Indians (NRIs).

Foreign Collaborators: If approved by the Government of India, large companies may be able to secure long term finance on the basis of collaboration agreements with companies abroad. Foreign collaboration may, thus, enable Indian companies to secure equity capital from abroad through the subscription of foreign collaborator to their share capital or by way of supply of technical knowledge, patents, drawings and designs of plants or supply of machinery.

International Financial Institutions: There are a number of international financial institutions which provide long-term funds for industrial development all over the world. The most important among them are: (i) The World Bank, and (ii) International Finance Corporation.

The World Bank grants loans for specific industrial projects of high priority included in the national development plan. The loans have to be guaranteed by the Government of India and may be given directly to an industrial concern or through a Government agency or may be given to the IOBI for refinancing to companies.

The International Finance Corporation (IFC) was established in 1956. It is an affiliate of the World Bank. As we know the World Bank grants loans only to government of member-countries or private enterprises with guarantee of the concerned government and it does not provide risk capital to enterprise in member-countries. IFC was set up to assist the private undertakings without the guarantee of the member-countries. It also provides them risk capital. IFC grants loans to industrial firms for a period of 8 to 10 years. Such loans do not require Government guarantee. Industrial concerns with investment plans drawn in accordance with the priority laid down under the national development plans can secure long-term loans from the IFC. But the corporation considers loan applications involving large amounts of about $100,000 or more from organizations having total assets of the value of at least $500,000.

Non-resident Indians: Persons of Indian origin and nationality living abroad (Non-resident Indians) are also permitted to subscribe to the shares and debentures issued by companies in India. A non-resident or a company controlled by a non-resident can invest upto a maximum of 5% of the paid up equity capital of an Indian company. New issues of shares or debentures by an industrial company can be subscribed by non-resident Indians to the extent of 40% of the new issue subject to a quantity ceiling of Rs. 40 lakh if the non-resident wants to have the option of repatriating the investment i.e. sell the shares and debentures and get the amount remitted abroad. However, exceptions are allowed in the case of priority industries like industrial machinery, scientific instruments, fertilizers, chemicals, drugs, export industry, hotels, etc.

(4) Retained Profits: An important source of long-term finance for ongoing profitable companies is the amount of profit which is accumulated as general reserve from year to year. To the extent profits are not distributed as dividend to the shareholders, the retained amount can be reinvested for expansion or diversification of business activities. It can also be used for renovation of assets or modernization of plant and equipment. It may be interpreted that the existing shareholders provide the finance. Hence, the company must decide to reinvest profits only when the rate of return is comparable with that of other similar companies. Moreover, a part of the profits must be distributed as dividend keeping in mind shareholders' expectation and the effect of dividend rate on the market price of shares. Retained profit is an internal source of finance. Hence it does not involve any cost of floatation which has to be incurred to raise finance from external sources. Further, the company does not have to face the uncertainties of external financing. The only drawback of this source of long-term finance is that it depends on the availability of adequate profits for retention.

Q8. Write a short note on followings:

(1) IFCI **(2) ICICI**

(3) IDBI **(4) UTI**

Ans. (1) IFCI (Industrial Finance Corporation of India): The main objective of IFCI is to render financial assistance to large-scale industrial units particularly at a time when the ordinary banks are not ready to assist these concerns.

Scope : The IFCI finances to these industrial concerns as a public limited company or a co-operative society engaged in manufacturing, preserving or processing of goods, generation or distribution of electricity and mining or hotel industry. Non-manufacturing concerns, private limited companies, partnerships and sole-traders are not financed by IFCI. But state-owned corporations incorporated as public limited company can get assistance from IFCI.

Following are the list of concerns that get financial assistance from IFCI :

(a) assembling, repairing or packaging of any article;
(b) repair, maintenance etc. of means of transport;
(c) transport of passengers or goods by roads, water or air;
(d) development of any area as an industrial estate; and
(e) providing technical knowledge or other services in promoting industrial growth.

Forms of Assistance: The following are the major forms of assistance provided by IFCI:

(a) Grant of loans or subscribing to debentures payable in not more than 25 years.
(b) Guaranteeing of (i) loans raised and (ii) debentures issued by the companies, scheduled bank and state co-operative banks payable within a period of 25 years and issue is made public.
(c) Underwriting the issues – shares, bonds and debentures.
(d) Subscribing the issues – shares.
(e) Guaranteeing deferred payments by importers of capital goods. But guarantee is provided only to those importers who are able to obtain the concession of deferred payment from foreign manufacturer or that from Indian manufacturer.
(f) Acting as an agent of the Central Government and the World Bank in respect of those loans which are sanctioned by them to industrial concerns. Minimum assistance of Rs. 30 lakh and maximum of Rs. 2 crores with 14% basic lending rate.

Purpose of Assistance:

(a) For establishment of new industrial undertaking.
(b) For expansion, modernization and rehabilitation of existing industrial undertakings.
(c) Loans for the purpose of working capital or for payment of existing liability in exceptional cases.

Procedure:

(a) First the application is filed along with all the technical and financial details with detailed project plan. Then the application received is processed and scrutiny is done.
(b) The examination of security offered.
(c) The disbursement of sanctioned assistance usually in installments over

period of the project construction.

(d) Lastly asking for progress report and assessment of progress by its own officials.

(2) ICICI : ICICI Bank (BSE: ICICI) (formerly **Industrial Credit and Investment Corporation of India**) is India's largest private sector bank in market capitalization and second largest overall in terms of assets. Bank has total assets of about USD 100 billion (at the end of March 2008), a network of over 1,399 branches, 22 regional offices and 49 regional processing centres, about 4,485 ATMs (at the end of September 2008), and 24 million customers (at the end of July 2007). ICICI Bank offers a wide range of banking products and financial services to corporate and retail customers through a variety of delivery channels and specialised subsidiaries and affiliates in the areas of investment banking, life and non-life insurance, venture capital and asset management. (These data are dynamic.) ICICI Bank is also the largest issuer of credit cards in India. ICICI Bank has got its equity shares listed on the stock exchanges at Kolkata and Vadodara, Mumbai and the National Stock Exchange of India Limited, and its ADRs on the New York Stock Exchange (NYSE).

The Bank is expanding in overseas markets and has the largest international balance sheet among Indian banks. ICICI Bank now has wholly-owned subsidiaries, branches and representatives offices in 18 countries, including an offshore unit in Mumbai. This includes wholly owned subsidiaries in Canada, Russia and the UK, offshore banking units in Bahrain and Singapore, an advisory branch in Dubai, branches in Belgium, Hong Kong and Sri Lanka, and representative offices in Bangladesh, China, Malaysia, Indonesia, South Africa, Thailand, the United Arab Emirates and USA. Overseas, the Bank is targeting the NRI (Non-Resident Indian) population in particular.

ICICI reported a 1.15% rise in net profit to Rs. 1,014.21 crore on a 1.29% increase in total income to Rs. 9,712.31 crore in Q2 September 2008 over Q2 September 2007.

(3) IDBI: The **Industrial Development Bank of India Limited** commonly known by its acronym **IDBI** is one of India's leading public sector banks and 4th largest Bank in overall ratings.

RBI categorised IDBI as "other public sector bank". It was established in 1964 by an Act of Parliament to provide credit and other facilities for the development of the fledgling Indian industry. It is currently the tenth largest development bank in the world. Some of the institutions built by IDBI are The National Stock Exchange of India (NSE), The National Securities Depository Services Ltd. (NSDL) and the Stock Holding Corporation of India (SHCIL)

IDBI BANK, as a private bank after government policy for new generation private banks.

(4) UTI: Unit Trust of India was created by the UTI Act passed by the Parliament in 1963.For more than two decades it remained the sole vehicle for investment in the capital market by the Indian citizens. In mid- 1980s public sector banks were allowed to open mutual funds. The real vibrancy and competition in the MF industry came with the setting up of the Regulator SEBI and its laying down the MF Regulations in 1993. UTI maintained its pre-eminent place till 2001, when a massive decline in the market indices and negative investor sentiments after Ketan Parekh scam created doubts about the capacity of UTI to meet its obligations to the investors. This was further compounded by two factors; namely, its flagship and largest scheme US 64 was sold and re-purchased not at intrinsic NAV but at artificial price and its Assured Return Schemes had promised returns as high as 18% over a period going up to two decades..!!

Fearing a run on the institution and possible impact on the whole market Government came out with a rescue package and change of management in 2001. Subsequently, the UTI Act was repealed and the institution was bifurcated into two parts .UTI Mutual Fund was created as a SEBI registered fund like any other mutual fund. The assets and liabilities of schemes where Government had to come out with a bail-out package were taken over directly by the Government in a new entity called Specified Undertaking of UTI, SUUTI. SUUTI holds over 27% stake Axis Bank. In order to distance Government from running a mutual fund the ownership was transferred to four institutions; namely SBI, LIC, BOB and PNB, each owning 25%. Certain reforms like improving the salary from PSU levels and effecting a VRS were carried out UTI lost its market dominance rapidly and by end of 2005, when the new share-holders actually paid the consideration money to Government its market share had come down to close to 10%!

A new board was constituted and a new management inducted. Systematic study of its problems role and functions was carried out with the help of a reputed international consultant. Fresh talent was recruited from the private market, organizational structure was changed to focus on newly emerging investor and distributor groups and massive changes in investor services and funds management carried out. Once again UTI has emerged as a serious player in the industry. Some of the funds have won famous awards, including the Best Infra Fund globally from Lipper. UTI has been able to benchmark its employee compensation to the best in the market, has introduced Performance Related Payouts and ESOPs.

The UTI Asset Management Company has its registered office at: UTI

Tower, Gn Block, Bandra - Kurla Complex, Bandra (East), Mumbai - 400 051.It has over 70 schemes in domestic MF space and has the largest investor base of over 9 million in the whole industry. It is present in over 450 districts of the country and has 100 branches called UTI Financial Centres or UFCs. About 50% of the total IFAs in the industry work for UTI in distributing its products! India Posts, PSU Banks and all the large Private and Foreign Banks have started distributing UTI products. The total average Assets Under Management (AUM) for the month of June 2008 was Rs. 530 billion and it ranked fourth. In terms of equity AUM it ranked second and in terms of Equity and Balanced Schemes AUM put together it ranked FIRST in the industry. This measure indicates its revenue- earning capacity and its financial strength.

Besides running domestic MF Schemes UTI AMC is also a registered portfolio manager under the SEBI (Portfolio Managers) Regulations. It runs different portfolios for is HNI and Institutional clients. It is also running a Sharia Compliant portfolio for its Offshore clients. UTI tied up with Shinsei Bank of Japan to run a large size India-centric portfolio for Japanese investors.

For its international operations UTI has set up its 100% subsidiary, UTI International Limited, registered in Guernsey, Channel Islands. It has branches in London, Dubai and Bahrain. It has set up a Joint Venture with Shinsei Bank in Singapore. The JV has got its license and has started its operations.

In the area of alternate assets, UTI has a 100% subsidiary called UTI Ventures at Banglore This company runs two successful funds with large international investors being active participants. UTI has also launched a Private Equity Infrastructure Fund along with HSH Nord Bank of Germany and Shinsei Bank of Japan.

Q9. What is meant by 'underwriting' of shares and debentures? Discuss briefly the terms and condition relating to underwriting.

[Dec 2006, Q1(d)] [June 2003, Q2]

Ans. Underwriting : The procedure by which an underwriter brings a new security issue to the investing public in an offering. In such a case, the underwriter will guarantee a certain price for a certain number of securities to the party that is issuing the security (in exchange for a fee). Thus, the issuer is secure that they will raise a certain minimum from the issue, while the underwriter bears the risk of the issue.

Underwriting refers to the process that a large financial service provider (bank, insurer, investment house) uses to assess the eligibility of a customer to receive their products (equity capital, insurance, mortgage or credit). The name derives from the Lloyd's of London insurance market. Financial bankers, who would accept some of the risk on a given venture (historically a sea voyage with associated risks of shipwreck) in exchange for a premium, would literally write their names under the risk information which was written on a Lloyd's slip created for this purpose.

Terms and Conditions of Underwriting : There is a written agreement between the company and the underwriter known as the 'Underwriting Agreement' (or Contract). Usually the following aspects are specified in this agreement :

(i) The number of shares or debentures which are agreed to be underwritten.

(ii) An undertaking by the underwriters to take up such of the shares or debentures as are not subscribed by the public.

(iii) An undertaking by the company that the terms of issue given in the prospectus will not be changed without the consent of underwriters.

(iv) Authority of the underwritings to the company to allot them the balance of shares or debentures not taken up by the public.

(v) The rate of commission to be paid to the underwriters and the mode of payment.

The commission is payable as a percentage of the issue price of all the shares or debentures even if the issue is fully subscribed by the public.

Sometimes the underwriters want to subscribe to a block of shares or debentures even if the total issue is fully subscribed by the public. This is known as 'firm offer'. A clause to that effect is that effect is then included in the underwriting agreement. Thereby the underwriters are assured of allotment of the block of shares or debentures specified for which they have made a firm offer.

Q10. What is a Stock Exchange? Briefly discuss the functions of stock exchanges. [Dec 2007, Q4]

Ans. A **stock exchange**, **securities exchange** or (in Europe) **bourse** is a corporation or mutual organization which provides "trading" facilities for stock brokers and traders, to trade stocks and other securities. Stock exchanges also provide facilities for the issue and redemption of securities as well as other financial instruments and capital events including the payment of income and dividends. The securities traded on a stock exchange include: shares issued by companies, unit trusts and other pooled investment products and bonds. To be able to trade a security on a certain stock exchange, it has to be *listed* there. Usually there is a central location at least for recordkeeping, but trade is less and less linked to such a physical place, as modern markets are electronic networks, which gives them advantages of speed and cost of transactions. Trade on an exchange is by members only. The initial offering of stocks and bonds to investors is by definition done in the primary market and subsequent trading is done in the secondary market. A stock exchange is often the most important component of a stock market. Supply and demand in stock markets is driven by various factors which, as in all free markets, affect the price of stocks.

Bombay Stock Exchange

There is usually no compulsion to issue stock via the stock exchange itself, nor must stock be subsequently traded on the exchange. Such trading is said to be *off exchange* or over-the-counter. This is the usual way that bonds are traded. Increasingly, stock exchanges are part of a global market for securities.

Functions of Stock Exchanges: Stock exchange, being a part of financial market, plays a very important role in the economic development of the country. The functions of Stock Exchanges may be enumerated as (a) primary functions, and (b) secondary functions.

Primary Functions:

(a) Marketability and price continuity: The stock exchange provides for easy marketability of securities as securities can be bought and sold conveniently on the floor of the stock exchange. Since transactions take place regularly, there is continuity in the dealings. Prices quoted are duly recorded and reported in the newspapers for the benefit of investing public. Besides, price fluctuations are also moderated because of the continuity of buying and selling.

(b) Mobilising surplus savings: Stock exchange is an integral part of the capital market of a country. It is because through stock exchanges the savings from all parts of the country are made available to the industrial and commercial undertakings for meeting their financial requirements.

(c) Barometer of economic and business conditions: The intensity of buying and selling of securities and the corresponding rise or fall in the prices of securities reflect the investors' assessment of the economic and business conditions. Thus, during periods of economic and business prosperity prices of securities tend to rise. Conversely, prices tend to fall when there is economic stagnation or when business activities slow down as a result of depression in the markets. Indeed, change in security prices are known to be highly sensitive to changing economic, social and political conditions. In the words of Alfred Marshall, the well known economist, stock exchanges are not merely the chief theatres of business transactions, they are also barometers which indicate the general conditions of the atmosphere of business.

(d) Mobility of capital: Stock exchanges furnish an open and continuous market for securities. Savings invested in securities are converted into cash for reinvestment in other securities. Thus, stock exchanges provide mobility to capital and facilitate sound investment.

(e) Contribution to capital formation: Savings are encouraged when people come to know about the avenues of investment. Stock markets educate investors as regards where and how to invest their savings for a fair return.

(f) Stock absorber: Stock exchanges bring about equilibrium in the prices of securities which are bought and sold by speculators. Speculators generally buy securities in anticipation of rise in the prices. As a result of their buying, prices do not decline as low as might have been the case without their buying. Again when prices are high, speculators sell securities in anticipation of decline in the prices. Their selling prevents price rising too high. Thus, speculative activities regulate excessive price fluctuations.

(g) Sifting process: Investors generally prefer to invest their savings after proper assessment of the relative risks and returns associated with different securities. The comparative advantages and disadvantages of investment in various types of securities may be grasped by investors from the dealings which take place on the stock exchanges. Hence they can pick and choose from among different securities and make investment decisions on a sound basis.

(h) Facilitates resource allocation: As a result of stock market transactions, funds flow from the less profitable to more profitable enterprises. Thus the existence of stock exchange provides for mobility of funds i.e. movement or flow of funds in the economy as a whole. Industries which have potentials of growth are able to attract the savings of people towards their ventures relatively more than those which have no such prospectus. Thus, financial resources of the economy are allocated on a reasonable basis. It is said that "without the stock exchange, the savings of the community, the sinews of economic progress and productive efficiency, would be used much less completely and be much more wasteful, than they are now".

Secondary Functions:

(a) Safety of investment and equity in dealings: The stock exchanges do not allow trading in each and every company's securities. Companies which want their securities to be traded on the floor of a stock exchange have to fulfill certain conditions. The stock exchange satisfies itself about the genuineness and soundness of the company to protect the investors from being cheated. There are a wide variety of securities. The investors have the opportunity to assess the relative advantages of investing in securities of companies dealing in various products (engineering goods, consumer goods, etc.) having wide markets and situated in different parts of the country. Every region or state and every industry gets a fair share of the investor's attention for investment of their savings.

(b) Easy liquidity: The investors usually prefer liquidity of their investment i.e., easy conversion into cash, besides adequate return on their investment. The stock markets provide that assurance to investors. These are markets which facilitate buying and selling of securities. As such the investors readily come forward to subscribe to new issues. Thus, stock exchange assures liquidity of investments which goes to serve the investor's need.

(c) Accurate and continuous report regarding sales: All stock exchanges maintain regular record of the securities traded each day and the prices at which deals are finalized. This information is supplied to newspapers and other information media alongwith the prices of important securities which ruled at closing time. The statistics relating to prices at which securities were traded are published in weekly bulletins for the information of the investors. This information helps in ascertaining the trend of price fluctuations and promotes healthy speculation.

(d) Full information regarding listed companies: The organized stock exchanges collect information about the companies listed with them and publish the information in the form of 'Official Year Book". This proves very useful to the investors in making investment decisions.

(e) Helpful in re-investment decisions: The investors sometimes want to switch their investments from one type of securities to others depending on which will be more rewarding. If shares or debentures of a company are in greater demand there is a rise in their market price indicating that the investors have assumed the company's performance and prospects to be better than others. On the other hand, if shares or debentures are offered for sale by many, the price tends to fall indicating that investors are not satisfied with the earnings and future prospects of the company. Thus, changes in the prices of securities provide a fair index of demand and supply of securities of particular companies. The investors can make their investment decisions accordingly.

(f) Safeguards to investors: Every stock exchange has its own rules and regulations for the control of operations of the exchange. Only members are allowed to deal in securities and make transactions. As the members have to transact their business strictly according to the rules, the investors' interests are safeguarded against dishonesty or malpractices.

Q11. Discuss the method of trading on a stock exchange.

Ans. Stock Exchange Trading: The term **'Stock Exchange Trading'** suggests the exchange of stocks or shares, or other securities of companies that are carried forward by brokers or traders of stocks. Parties concerned with stock trading can be an individual or a company. The market for such exchanges is called **Stock Exchange**.

A **stock exchange** is the chief component of a **stock market. Supply and demand forces in stock markets** is guided by various factors which, as in all free markets, affect the price of stocks. **Stock Exchanges** also provide facilities for the issue and redemption of securities as well as other financial instruments and capital events including the payment of income and dividends. The securities involved in **Stock Exchange Trading** include :

- Shares issued by companies
- Unit trusts
- Other pooled investment products like bonds

In order to indulge into **Stock Exchange Trading**, a company has to enlist itself under a stock exchange. Usually there is a central location at least for record keeping. However, riding the success of technology, modern markets are electronic networks have raised the speed and cost of transactions.

Stocks and bonds are offered initially to investors is done in the primary market. Henceforth, trading is carried out in the secondary market.

This is the usual way that bonds are traded. **Trading at stock exchanges** is gradually becoming a part of a **global market for securities**.

Stock Exchange Trading has multiple roles in the functioning of an economy. Such diverse roles played by stock exchanges include, generation of initial capital required for starting a business, channelizing savings for further investment, facilitating growth of a company, redistributing funds of the company, and creating **investment opportunities** for small investors.

Stock Exchanges act as barometers of the economy since the movement of share prices and in general of the stock indexes indicate the general trend in the economy.

Thus despite involving a tremendous amount of risk, **Stock Exchange Trading** is gaining popularity day-by-day.

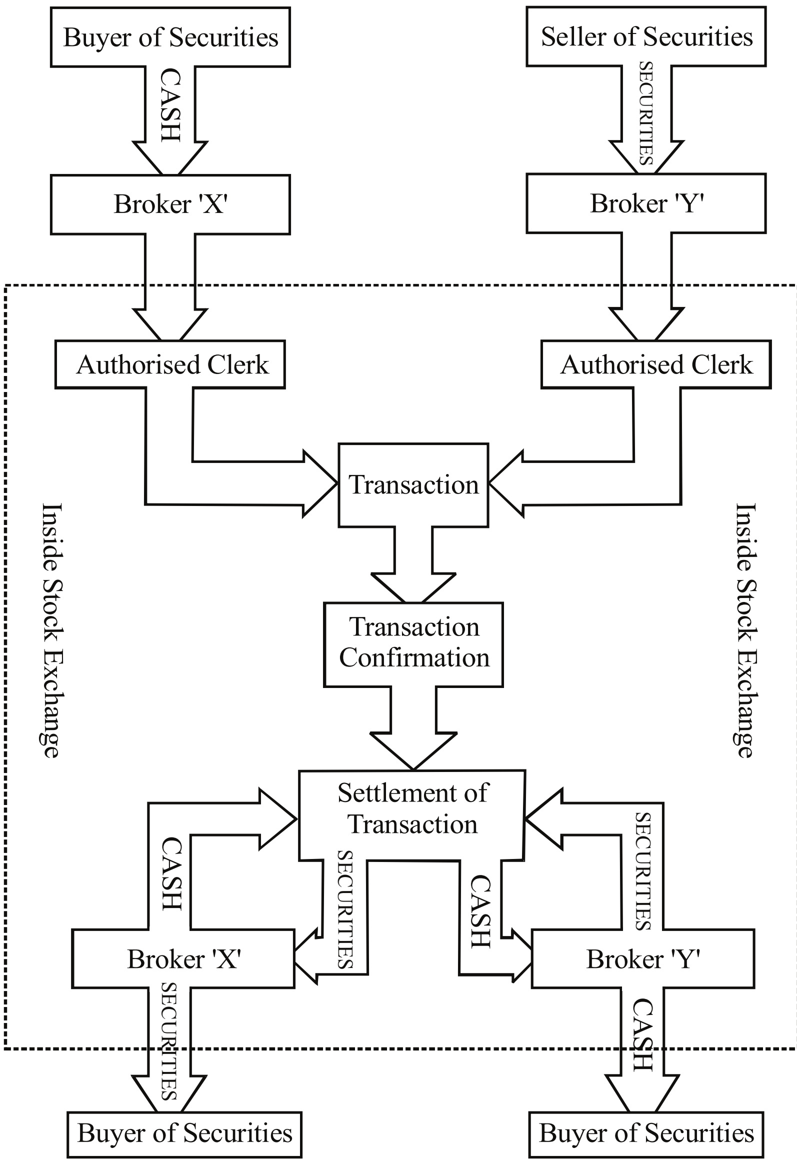
Q12. Write a short note on various types of dealing in stock exchange.

Ans. There are various types of dealing in stock exchanges:

(a) Spot delivery contracts: Such contracts are settled on the spot i.e., the delivery and payment are made on the day of the transaction itself or latest by the following day. It is not a common practice now-a-days.

(b) Ready delivery contracts: Such contracts are settled within a short period of time. Usually the period allowed is twelve days and the settlement takes place on the following settlement day. No postponement is allowed in case of ready delivery contracts.

Fig : The Process of Purchase and Sale of Securities in the Stock Exchange



(c) Forward Delivery Contracts: Such contracts are also due for settlement on the following settlement day but they can be postponed to the next settlement day, if so desired. This facility is provided by the stock exchange only in those scripts which are included in the specified list (List A). Such transactions are meant for speculation where the buyer has no intention to take delivery and make payment. He simply covers it by another transaction and earns or loses the difference in prices.

For example Mr. Prakash buys 1,000 shares of Reddy Motors at Rs. 50 per share in the hope that its price will go up. If the price rises as expected, he will settle it by a transaction for sale of 1,000 shares and pocket the difference. If the price falls, he may decide to settle it by a transaction for sale at a lower price and pay the difference. Alternatively, expecting the price to rise, he may seek postponement of its settlement to the next settlement day by paying the necessary charges. Technically, such postponement is known as **'Carry Over' or 'Badla'** and the charges paid are called **'badla charges'**. Sometimes the professional badlawalas may advance the necessary sum of money to finance purchase of shares by the bull speculator at certain rate of interest and thus help him to postpone the sale.

Forward delivery contract is not the same thing as future trading. Future trading means entering into a transaction to sell or buy at a future date. This kind of trading is prohibited in India.

Q13. What do you know about the terms used in stock exchanges/ market?

Ans. The terminology used by the operators on the stock exchange is somewhat different from what is commonly used in business.

Bull or Long : A person who buys securities in the expectation of a rise in their prices, is called 'Bull'. He becomes active whenever there is anticipation of a rise in the prices of securities. He buys with the object of selling them in future. He is also known as **tejiwala**. If his expectations come true, he earns a profit. If the market goes against his expectation, he incurs a loss. Suppose, he makes a deal for purchase of 100 shares at Rs. 105, expecting it will go up. On the settlement day the price of the share rises to Rs. 110. He informs his broker to settle the deal. He earns a profit of Rs. 500. On the other hand, if the market price of the share goes down he may incur a loss on settlement of the transaction. In such a situation he can postpone the settlement due to unfavourable price by paying budla charges (also called contango). He is called 'bull' as he has a tendency to raise the price artificially like a bull who generally throws his victim upwards.

Bear : A person who sells short i.e., sells what he does not possess at the time of selling, is called a 'Bear'. He does so in the hope of buying at a lower price at the time of delivery. Thus a bear anticipating a fall in price in future sells at the current price which is high. If his expectations come true, he gains, otherwise he loses. If the market goes against him i.e. if the market prices rises, he can postpone his settlement by paying badla charges (also called backwardation). A sale of securities by bears is called 'short selling'. He has to buy them from the market for making delivery to the buyer.

Stag: A person is called a 'stag' if he deals in the new issues of companies. He applies for shares on the basis of prospectus and sells these shares at a premium soon after the allotment is made to him. He is just like a bull, since he also foresees a rise in the price of the securities. He applies for a big allotment, since he has to pay only application money to the company at the time of application. A stag sometimes creates artificial demand for the securities in the market so as to cause a rise in their prices. If the response for such shares is poor and he is allotted all the shares applied for, then he has to sell these shares at a discount. In such conditions he sustains loss.

Contango: Budla charges paid by a bull to the broker for carrying over his transaction to the next settlement date, is called 'contango'. Contango amount depends upon the class of securities, their quantity, value and interest rates prevailing in the market at the time of transaction. Usually it is equivalent to the 'middle price' of the difference between the agreed price and the market price prevailing on the day of the settlement.

Backwardation: This is also a type of badla charge payable to the bull by the bear seeking postponement of the transaction to the next settlement date.

Cum-Dividend: Cum means 'with' or 'including'. Where shares are quoted as Cum-Dividend, the buyer gets a right to receive the dividend on such shares which is payable after the date of sale. The purchase price includes the amount of dividend due. This is because the buyer becomes a registered shareholder and he is entitled to get dividend as and when it is declared by the company. Most transactions in securities are cum-dividend.

Ex-Dividend: The term refers to the price of shares purchased without the right to get the dividend from the company. The dividend declared or accrued is payable to the person whose name appears in the books of the company. Hence, when the buyer purchases the shares after the closure of the books of the company, he buys them ex-dividend.

Concerning: Concerning refers to the condition in the market in which almost the entire supply of a particular security is held by an individual or a group of individuals. In such a situation the bears find it difficult to buy them to meet their commitments of delivering the scripts. This term also refers to purchase of securities by an outsider in large quantities in order to oust the existing management of a company or to put them in an embarrassing situation.

Margin Trading: It refers to the practice of buying and selling securities by depositing with the broker a certain percentage of the value of the securities involved in the transaction. The percentage of value so deposited is called 'Margin Money' or 'Margin'. The objective is to meet the loss, if any, out of this deposit. When the margin money is deposited, the broker credits the Margin Account of the customer. Deposit of margin money is a precondition for the securities to be held on account of the client. Where the margin falls short of the amount of loss suffered by the client on the securities held in his account, the broker may ask the client to deposit additional amount to cover the shortfall. In case he does not deposit such amount, the broker can sell the securities and recover the amount.

Arbitrage: Buying in one market where the price is low and selling the same securities in another market where the price is comparatively higher is termed as 'Arbitrage Operation'. Such dealings confer all the benefits of a continuous market and bring the divergent prices of various stock exchanges to a uniform level. The scope of operations of the stock exchange is also expanded through such operations. The prices are equalized subject to the cost of communication and transfer of funds from one place to another.

Rigging the Market: When the prices of particular shares are artificially forced up in the market, it is known as 'Rigging'. This is generally the result of activities of bulls (speculative buyers) who raise the demand and thereby push up the market price. Those who hold large blocks of shares often buy and sell to make the market active and then gradually unload their holdings at a profit.

Settlement Day: In every stock exchange a particular day is fixed for the settlement of transactions between buyers and sellers. This day may be every Monday or every Saturday of the week. In other words, there is a weekly settlement. The speculators may settle their deals on a particular settlement day or postpone it to the next settlement day on payment of the 'badla' charges. As stated earlier, postponement of settlement is allowed only in case of shares included in the specified list (List A) of the stock exchange concerned.

Blank Transfer: When shares are sold, the seller has to sign a transfer deed giving necessary particulars about the shares and the transferee. It also involves stamp duty which is payable at the prescribed rates. When the deed is filed with the company, the transfer is duly registered and the name of the transferee is recorded in place of that of the transferor. However, when the seller signs the transfer deed without filling in the name of the transferee it is known as 'blank transfer'. This type of transfer is found to be convenient where the speculators carry over their deals involving temporary purchase and sale of securities. Blank transfer permits speculators to buy and sell securities without paying stamp duty for some time. This tends to encourage excessive speculation. Hence, to discourage blank transfers it is required that the transfer deed in a prescribed form must be presented to the Registrar of Companies before it is signed by the transferor. The date of presentation is endorsed on the deed. Thereafter, the transfer deed must be delivered to the company for registration of the transfer within a certain period. In the case of listed securities, it must be delivered before the first closure of the Register of Members after the date of presentation endorsed on it. In the case of non-listed securities the deed must be delivered within two months from the date of presentation endorsed on it.

List A Securities or Specified Securities: In every stock exchange, there are certain specified securities in respect of which carry over facility is permitted. These securities are known as 'List A Securities' or 'Specified Securities'.

List B Securities or Cash Securities: Securities other than List A Securities are known as 'List B Securities' or 'Cash Securities'. The transactions in such securities have to be settled within a limited period. No postponement is allowed.

Jobber: There are two types of members in the London Stock Exchange known as brokers and jobbers. Every member of the London Stock Exchange has to declare whether he will act as a broker or a jobber. A broker is to act on behalf of the customers and derive his income through the commission he will charge on the purchase and sale of the securities. He is not allowed to buy or sell in his own name. The jobber, on the other hand, is an independent dealer in securities. He can purchase and sell securities in his own name and deal with a broker or with another jobber. He does not work on behalf of non-members. The distinction between a broker and a jobber is not followed in India. The member of the stock exchange can act as a broker and also buy and sell in his own name. at the Bombay Stock Exchange the members are unofficially divided into two categories: (i) **brokers**, and (ii) **tarawaniwalas**. A member who acts both as a broker and a jobber is known as 'Tarawaniwala'. In India most members fall in this category.

Q14. What do you mean by listing?

[June 2005, Q1(f)] [June 2003, Q2]

Ans. Listing means admission of the securities to dealings on a recognised stock exchange. The securities may be of any public limited company, Central or State Government, quasi governmental and other financial institutions/ corporations, municipalities, etc.

The objectives of listing are mainly to :

- provide liquidity to securities;
- mobilize savings for economic development;
- protect interest of investors by ensuring full disclosures.

The Exchange has a separate Listing Department to grant approval for listing of securities of companies in accordance with the provisions of the

Securities Contracts (Regulation) Act, 1956, Securities Contracts (Regulation) Rules, 1957, Companies Act 1956, Guidelines issued by SEBI and Rules, Bye-laws and Regulations of the Exchange.

Finance minister in Dalaal street

A company intending to have its securities listed on the Exchange has to comply with the listing requirements prescribed by the Exchange, which are as under :

New Companies

Companies listed on other stock exchanges

Companies delisted by this Exchange seeking relisting on this Exchange

Minimum Number of Shareholders

Permission to use the name of the Exchange in an issuer Company prospectus

Submission of Letter of Application

Allotment of Securities

Allotment Letters/Certificates and Trading Permission

1% Security Deposit.

Listing Fees

Compliance with Listing Agreement

"Z" Group

One Window Clearance

(a) New Companies

(i) Minimum Capital: New companies can be listed on the Exchange, if their Issued & Subscribed Equity Capital after the public issue, is Rs.10 crores and above.

(ii) Minimum Public Offer: As per Rule 19(2) (b) of the Securities Contracts (Regulation) Rules, 1957, securities of a company can be listed on a Stock Exchange only when at least 25% of each class or kind of securities is offered to the public for subscription. For this purpose, the term "offered to the public" means only the portion offered to the public and does not include reservations of securities on firm or competitive basis.

SEBI may, however, relax this condition on the basis of recommendations of stock exchange(s), only in respect of a Government company defined under Section 617 of the Companies Act, 1956.

(b) Companies listed on other stock exchanges: The companies listed on other Stock Exchanges and seeking listing on this Exchange are required to fulfill the following criteria:

(i) Minimum Issued Equity Capital of Rs.3 crores to Rs.10 crores;

(ii) Profit track record for atleast three years;

(iii) Minimum Market Capitalisation of Rs.20 Crores, based on average price of last six months;

(iii) Trading for a minimum 50% of the total trading days during the same six months on any stock exchange;

(iv) Minimum average volume traded per day during the last three complete months should be 500 shares and minimum 5 trades per day;

(v) 25% of the issued capital should be with public (including body Corporates) and minimum 15 shareholders per Rs. 1 lakh of capital in the public category.

(c) Companies delisted by this Exchange seeking relisting on this Exchange : The companies delisted by this Exchange and seeking relisting are required to have a minimum Issued & Subscribed Equity Capital of Rs.10 crores.

Minimum Number of Shareholders: The public offer should result in a wide distribution of shares among the general public and there should be minimum 25% of the company. S issued capital with the public (inclusive of corporate bodies) and at least 5 public shareholders for every Rs.1 lakh of net capital offered to the public after public issue and at least 10 public shareholders for every Rs.1 lakh of equity offered to the public through offer for sale. .

For this purpose, a public shareholder means a person who is neither a promoter nor does he hold more than 1% of the equity capital of the company. This is also a continuous listing requirement.

Permission to use the name of the Exchange in an Issuer Company's prospectus: The Exchange has started a procedure in terms of which the companies desiring to list their securities offered through public issues are required to obtain its prior permission to use the name of the Exchange in their prospectus or offer for sale. Documents before filing the same with the concerned office of the Registrar of Companies. The Exchange has since last two years formed a "Prospectus Scrutiny Committee" to analyse draft prospectus/offer documents of the companies in respect of their forthcoming public issues of securities and decide upon the matter of granting them permission to use the name of "The Stock Exchange, Mumbai" in their prospectus/offer documents. The Committee evaluates the promoters, company, project and several other factors before taking decision in this regard.

Submission of Letter of Application: As per Section 73 of the Companies Act, 1956, a company seeking listing of its securities on the Exchanges is required to submit a Letter of Application to all the Stock Exchanges where it proposes to have its securities listed before filing the prospectus with the Registrar of Companies.

Q15. What are the reasons of passing the securities contractors (Regulation) Act, 1956?

Ans. The members of the stock exchange, brokers, investors and speculators are the people who engage in stock market operations. All these people derive advantages from the working of the market. However, stock markets suffered from a number of evils in the past and were regarded as gambling dens of the brokers.

The attention of the Government was drawn from time to time to the ills of stock markets as a result of which the Securities Contracts (Regulation) Act, was passed in 1956 to regulate and control stock market operations in the wider interests of the financial markets, institutions and the public. The main provisions of this Act are as follows:

(a) There shall be only one recognized stock exchange in one region. This will have a unitary control.

(b) Dealers and brokers outside the area of the recognized stock exchange will be licensed.

(c) A recognized stock exchange shall be entitled to frame its own bye-laws for regulation and control of contracts subject to the approval of the Central Government. The bye-laws may regulate (i) opening and closing of market; (ii) regulation of trading hours; (iii) establishment of clearing house; (iv) regulation of prohibition of blank transfer (now these are regulated by the Companies Act); (v) listing of securities on the stock exchange; (vi) regulation or prohibition of carry over or budla system; (vii) limitations on the volume of trading by members and on their open positions; (viii) fixing minimum and maximum prices for securities in emergencies; and (ix) separation of functions of jobbers and brokers and regulation of tarawani (jobbing) business.

(d) The Central Government is empowered to make and amend bye-laws after consulting the governing bodies of these exchanges.

(e) Dealings in future are prohibited, since they are regarded as gambling contracts.

(f) The Central Government has a right to withdraw recognition to or supersede, the governing body of the exchange in abnormal situations.

(g) A recognized stock exchange must submit periodical returns relating to its affairs and give information as required by the Government from time to time.

(h) Central Government has wide powers relating to the listing of securities. It can compel any public limited company to list its securities. It can vary or set aside the refusal of a stock exchange to list securities on an appeal made by a company.

The Government of India has recently set up a high-power body known as the Securities Exchange Board of India which will provide necessary guidance for the healthy and orderly development of securities markets which will instill confidence among the investors and provide adequate protection to them.

Chapter-3

Marketing

Q1. Define Advertising. What is the difference between advertising and publicity? [June 2003, Q4(a)]

Ans. Advertising is known to each one of us. This is so because right from morning till night we come across a number of them in newspapers, in magazines, on the roads as hoardings, in shops as posters, in films and on TV. In fact, in stares at us from all sides and is all-pervasive. What function does it perform essentially? It influences our decisions, especially buying decisions.

If you want to see the effect of advertising ask a nursery going child these days he/she are aware of brands like Colgate and Rasna and Nirma thanks to TV advertising. Jingles of the products are hummed by the young and old alike. Advertising puts across the message in a convincing way, and guides us to take action-buy these products repeatedly.

Now Let's first understand the definition of advertising. The word advertising has its origin from a Latin word 'advertire' which means to turn to.

The dictionary meaning of the word is 'to announce publicly or to give public notice.'

American Marketing association has defined advertising as "any paid form of non-personal presentation and promotion of ideas, goods and services by an identified sponsor."

Advertising is a paid form of communication, although some forms of advertising, such as public service announcements (PSAs), are donated space and time.

Second, not only is the message paid for, but also the sponsor is identified.

Third, most advertising tries to persuade or influence the consumer to do something. Although in some cases the point of the message is simply to make consumers aware of the product or company.

Fourth and fifth, the message is conveyed through many different kinds of mass media reaching a large audience of potential consumers.

Finally, because advertising is a form of mass communication, it is also non-personal.

A definition of advertising, then, includes all six features. Advertising is paid non-personal communication from an identified sponsor using mass media to persuade or influence an audience.

In an ideal world every manufacturer would be able to talk one-one with every consumer about the product or service being offered for sale. Personal selling is typically a one-on-one approach, but it is very expensive.

Although advertising delivered through interactive technology might be considered personal rather than mass communication, it is still a far cry from personal selling. Advertises can provide more customization through interactive media such as the World Wide Web, but it is not the same as meeting with every customer individually to discuss a product or service. The key point is that interactive advertising reaches a large audience just like traditional advertising.

The costs for time in broadcast media, for space in print media, and for time and space in interactive and support media are spread over the tremendous number of people that these media reach. For example, \$1.2 million may sound like a lot of money for one Super Bowl ad; but when you consider that the advertisers are reaching over 500 million people, the cost is not so extreme.

Advertising versus Publicity: Advertising is the obvious way to promote a business or product. Once you learn the techniques of creating and testing great ads, and the right places to advertise - it can produce results - but at the end of day, your results will depend directly to the amount of advertising space you buy, which is itself dependent on your advertising budget. Publicity is the smart way to promote a business or product. Good publicity allows you to achieve results totally disproportionate to the amount of money and effort put in.

This chart compares these two marketing techniques :

Advertising	Publicity
Expensive You pay for every placement of your ad. Which is obviously going to expensive if you want a lot of exposure.	**Cost-Effective** A great story can snowball. Editors may be failing over themselves to cover your company or products. Imagine getting statewide, nationwide or even international exposure, absolutely free.
In "The Advertising Ghetto" Most media clearly separate advertising from editorial. Many readers will therefore find ways to either avoid reading your ad completely, or if they do read it will read it with loss interest.	**You're the Story** Generally readers buy newspapers to read the news. They buy magazines to read the articles. If you're featured, they will read about you.
Lack of Credibility Do you believe everything said in advertisements?	**Strong Credibility** Readers trust independent authority, figures including reviewers, columnists, journalists and broadcasters. An article about your business has far more credibility than an advertisement ever could have.

Q2. What are the various objectives served by advertisements?

Ans. Advertising objectives are the communication tasks to be accomplished with specific customers that a company is trying to reach during a particular time frame. A company that advertises usually strives to achieve one of four advertising objectives: trial, continuity, brand switching, and switchback. Which of the four advertising objectives is selected usually depends on where the product is in its life cycle.

Trial: The purpose of the trial objective is to encourage customers to make an initial purchase of a new product. Companies will typically employ creative advertising strategies in order to cut through other competing advertisements. The reason is simple: Without that first trial of a product by customers, there will not be any repeat purchases.

Continuity: Continuity advertising is a strategy to keep current customers using a particular product. Existing customers are targeted and are usually provided new and different information about a product that is designed to build consumer loyalty.

Brand Switching: Companies adopt brand switching as an objective when they want customers to switch from competitors' brands to their brands. A common strategy is for a company to compare product price or quality in order to convince customers to switch to its product brand.

Switchback: Companies subscribe to this advertising objective when they want to get back former users of their product brand. A company might highlight new product features, price reductions, or other important product information in order to get former customers of its product to switchback.

Q3. Explain the role of advertisements in the society.

[June 2006, Q7]

Ans. Advertising has affected not the core cultural values but the subsidiary cultural Lets start with the help of an example like to get married is a core cultural value. Advertising cannot effectively change it by telling people that you do not marry. Yes, to marry late and not at an early age is a subsidiary cultural value. Advertising can definitely affect it. It can persuade people to marry late. Advertisement is a mirror of the society in which it operates. It reflects the cultural values of that society.

In fact you will notice that some people argue that advertising debases our cultural standards. There are many factors, which affect culture and get affected by them like schools, colleges, families, museums, churches etc. Successful advertising is consistent with the cultural values of a given society. Yes, it can transfer some cultural values of one society to another society at a given point of time. Its cross-cultural impact will depend upon the universalisation of appeal.

Quit Smoking Advertisement

Advertising has improved our standards of living. We have realised how comfortable we could are in presence of AC, pressure pans and cookers, compact discs (CD's) and music systems, autos and two-wheelers, polyesters and popcorns, ballpoint pens and antibiotics. We have used these articles after getting interested in them through advertising. We've accepted some new ideas like microwave cooking, electric shaving; bucket washing through detergents etc. through advertising. All of us know that it has created new markets. It has contributed to our standard of living substantially.

Whenever we are talking about getting the new product into the market it is with the help of advertising we are confident about its function, quality, price and availability.

Advertising promises a quality, and forces manufacturers to live epic the promised, quality. So advertisement brings out consumer welfare by two-fold method :

(a) By improving standard of living.

(b) By improving product quality.

Advertisements for social causes like cancer prevention, Anti dowry campaign, family planning etc. make us socially responsible. It also protects consumers by educating them and by forcing the manufacturers to maintain a quality and be fair.

Q4. What are the characteristics of good advertisements?

[June 2005, Q1(c)] [June 2003, Q3(b)]

Ans. Designing an effective advertisement is a challenging task. There is no definite formula for that purpose. But certain guidelines may be kept in view while designing an advertisement. The essential characteristics of a good advertisement may be divided into two broad categories:

(1) Features Relating to the Message: The impact of an advertisement depends not only upon what is said about the product, but also how it is said. The message should be such as to win the attention and interest of the target audience. So, while designing the advertisement message, one should keep the following points in mind:

(a) Desirability: The message should say something desirable and interesting about the product. Otherwise, the advertisement may fail to induce the customers to buy the product.

(b) Exclusive: Customers should know how the product advertised is better than the other products. So, the advertisement message should point out the unique features of the product. In other words, it should say something exclusive or distinctive about the product which does not apply to any other brand in that product category. Then only people may realize why and how the product is better than others.

(c) Believable: Whatever is stated in the message should be believable. For instance, if the message conveys imaginary qualities of any product, people will never take the advertisement seriously. The message should actually compare with the product which the customer may verify so as to be convinced. Therefore, the message should be believable and provable.

(d) Attractive: If the message is attractive, it will draw the attention of the customers very easily. If the message is not catchy, it will not have any effect on the minds of people. Therefore, such words or pictures which may draw the attention of customers should be used in the advertisement.

(e) Memorable and easy to recall: The message should be easy to remember, so that it may be easy to recall it. Whenever customers go for shopping, the advertisement message should come to their mind and remind them about the product. Therefore, the words used in the message should be easy to memorise and recall.

Features Relating to Consumer Reach: Apart from the message, the impact of an advertisement also depends on how well it reaches the target customers. For this purpose, the following points should be borne in mind while designing the advertisement.

(a) Appropriate media: The advertisement message should be presented through the media to which the target customers have access. For example, if the majority of the target customers do not have television sets, the message presented by TV transmission will not reach them. Similarly, if the majority of customers are illiterate, the message presented in newspapers may not reach them. So, the use of appropriate media is highly important for the effectiveness of advertisements.

(b) Frequency: Frequency refers to the number of times any advertisement is repeated within a specified period of time. It also refers to the time gap between two or more advertisements. In other words, it refers to how many times and at what intervals the advertisement is repeated. The main purpose of repetition is to keep the message alive in the memory of the customers. If the frequency is less, people may not remember the message. If the frequency is more, people may get irritated and may stop giving attention to it. So, the frequency should be optimum.

(c) Timing : The specific time of advertising the message is an equally important aspect of advertisement. For example, if the advertisement appears on the T.V. when most of the customers are not viewing it, the effect will be much less as compared with the effect when a majority of the customers are viewing the T.V. programme. Hence, the timing of the advertisement should be so determined that it may reach the majority of customers.

Q5. Define Media. Discuss the types of media. [Dec 2003, Q6]

Ans. Communication is the art of transmitting information, ideas and attitudes from one point or person to another. Each of us communicates with another individual by directing a message to one or more of his senses – sight, sound touch taste speech or smell. When we smile, we communicate a desire for friendliness; the tone in which we say 'good morning' can indicate feelings all the ways from hostility to warm pleasure and the words we choose in speaking or writing convey a message we want to put across to other person. The more effectively we select and deliver those words, the better is our communication with him or her.

Contemporary society is far too complex to function only through direct communication between one individual and another. Our important messages to be effective must reach many people at a time. For example, a housewife who is angry at the frequent load shedding of electricity may talk to half a dozen neighbours about organizing a boycott. But if the editor of a local newspaper publishes a letter she writes, she writes, she communicates her idea to hundreds of women in a short time. We can take another example of a politician contesting for election, he spends much of his campaign time visiting people personally, holding meetings in the hope of winning their votes. Now, he hires time on television and radio, buys space in the newspapers, trying to deliver his message to thousands of voters simultaneously.

Let us now define mass media. The mass media is defined as the technological means of sending information, ideas, opinions etc. through the mass communication device to a diverse audience. In one sense, words and pictures are the media by which thought and feelings are communicated but medium need not be restricted to this meaning. Medium means something intermediates, a middle state, something that intervenes. For example, money is a medium of exchange between a buyer and seller. Stone is a medium for sculptors' recreation. A medium of communication can be any such item for transmission or transference of thought and feeling. Thus we can say, communication is an act or process involving transmission of information, ideas, emotions, skills etc., by the use of verbal or non-verbal means (words, pictures, figures, graphs, gestures, facial expression etc.).

Q6. Which are the factors that influence the choice of media?
[Dec 2004, Q6] [June 2003, Q3(b)]

Ans. The following factors influence the choice of media :

(1) Character of the medium
(2) Nature of the product to be advertised
(3) Type of audience
(4) Coverage
(5) Cost

(1) Character of the medium: To judge the suitability of any medium, the characters of different types of media should be analysed on a factual basis. The following aspects of the media are to be considered before choosing any particular medium.

(a) The geographical coverage of the medium i.e. national, regional or local.
(b) The frequency and duration of exposure of the message to the audience.
(c) Method of communication i.e., visual, oral, both visual and oral, etc.
(d) Power of the medium to reach special categories of audience e.g. children, ladies, business executives, etc. This is also called audience selectivity.
(e) Scheduling flexibility is another factor. Producing a TV advertisement takes more time than producing a newspaper advertisement. Similarly, withdrawal of advertisement with a short notice is not possible with some media.
(f) Production quality of the media.
(g) Degree of performance or durability in the sense that how long the advertisement can remain before prospective customers' eyes or within their grasp. A TV advertisement disappears within a few seconds whereas an hoarding continues delivering the same message to the passing public for a year or more.

Thus for a large manufacturer, a medium with the national coverage will be more suitable. To build up brand image, frequency of exposure may be more important than duration of exposure. On the other hand, to provide very detailed information about the product, duration may be more important. Demonstrating the usefulness of Polaroid camera may require a medium to make oral and visual presentation. To advertise ladies garments it may be useful to select women's magazines like the Femina or Women's Era.

(2) Nature of the product: Consumer goods need to be advertised with different types of appeal for effectiveness. Familiar goods of daily consumption do not require elaborate description, while industrial machinery may require technical details to be explained. The size of advertisement and the time of exposure required vary according to the nature of the products. Again, advertisement for consumer goods can reach the largest possible number of people through mass media like newspapers, radio and television. But industrial goods may be more effectively advertised through trade and technical magazines. Advertisement of garments is best done in multi-colour printing in magazines.

(3) Type of audience: Media habits of the target audience to be reached is one of the important factors to be considered while selecting the medium. If the target audience are illiterate, press medium (newspapers and magazines) is ineffective. Similarly, if the target customers are in villages where there are no TV sets, advertising by TV is a waste. The most effective medium to reach housewives in the urban areas may be the radio or television and for business executives it may be a professional magazine. Therefore, the characteristics of the target customers with respect to media are very important in selecting proper medium.

(4) Coverage: How many and what percentage of the potential buyers can be approached through each possible medium are also determining factors in the choice of a medium. One medium may be able to reach more number of target customers than the other media. Therefore, a medium which can reach the maximum number of target customers should be preferred. For instance, if target audience are illiterate and do not have TV sets, short films in the cinema halls may be more effective. Similarly, the number of doctors who can be reached through direct mail is expected to be more than the number who can be reached through any other medium. To advertise sewing machines to the urban customers, women's magazines may be more appropriate as the appeal will reach many more ladies through this medium.

(5) Cost: The most important factor determining the choice of a medium is the cost involved. Cost of a medium may be analysed in two ways: (1) absolute cost, and (2) cost related to audience size. Absolute cost is the actual charge for buying a certain amount of time or space in a medium. If the small firm had set aside a small amount for advertising, it cannot afford to use an expensive medium. For instance TV is a very expensive medium whereas newspaper advertising is relatively cheaper. However, what is important is not the absolute cost of using each medium but the size of the target audience reached in relation to the cost. Relative cost is a comparative cost. It is the absolute cost related to the size of the audience served by the chosen medium. For instance, charges for a full page advertisement in two different magazines may be exactly the same. But if one magazine has a circulation of 3 lakh and the other has a circulation of 4 lakh, advertisers choose the second magazine as it reaches more number of customers for the same money.

Q7. What is a channel of distribution? Explain briefly the channels of distribution used for consumer goods and industrial goods.

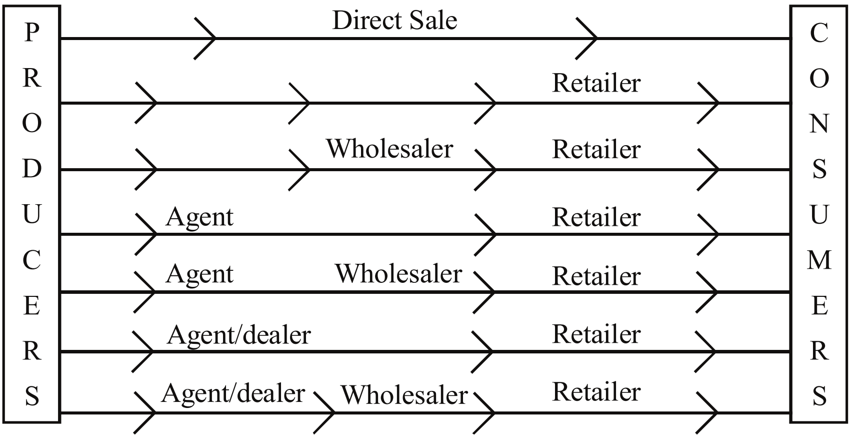
[Dec 2003, Q1(c)]

Ans. Channel of distribution - Meaning: A channel of distribution or trade channel is the path or route along which goods move from producers to ultimate consumers or industrial users. In other words, it is the distribution network through which a producer puts his product in the hands of actual users. The channel of distribution includes the original producer, the final buyer and any middlemen-either wholesaler or retailer. The term middleman refers to any institution or individual in the channel which either acquires title to the goods or negotiates or sells in the capacity of an agent or broker. But facilitating agencies who perform or assist in marketing function are not included as middlemen in the channel of distribution. This is because they neither acquire title to the goods nor negotiate purchase or sale. Such facilitating agencies include banks, railways, roadways, warehouses, insurance companies, advertising agencies, etc.

Q8. Describe the factors that influence the choice of distribution channel. **[June 2008, Q5] [Dec 2004, Q4]**

Ans. A channel of distribution or trade channel is the path or route along which goods move from producers to ultimate consumers or industrial users. In other words, it is the distribution network through which a producer puts his product in the hands of actual users. The channel of distribution includes the original producer, the final buyer and any middlemen-either wholesaler or retailer. The term middleman refers to any institution or individual in the channel which either acquires title to the goods or negotiates or sells in the capacity of an agent or broker. But facilitating agencies who perform or assist in marketing

function are not included as middlemen in the channel of distribution. This is because they neither acquire title to the goods nor negotiate purchase or sale. Such facilitating agencies include banks, railways, roadways, warehouses, insurance companies, advertising agencies, etc. The following diagram (chart) is illustrative of the channel of distribution which may exist in a market.



The above chart indicates that the number of middlemen may vary. If there is direct sale by the produce to the consumers then there is no middleman. But that is very rare. As the chart shows the producer may sell goods to retailer who may then sell the same to consumers. The producer may sell goods to wholesalers who may inturn sell to retailers and the retailer may sell to consumers. The fourth alternative channel of distribution is when any agent/dealer intervenes between the producer and retailers and acts as a middlemen. The agent is appointed by the producer for the sale of goods to the retailers. Another alternative channel is there when producer's agent sells goods to wholesalers who sell to retailers. Agent/dealer is an independent person/firm buying goods and selling them to retailers. Agent/dealer may also sell to wholesalers who may then sell to retailers and goods are thus made available to consumers. In the channel of distribution there may be more than one agent/dealer and wholesaler.

Choice of a channel of distribution: The factors to be considered before choosing a suitable channel of distribution are listed below:

(a) Product considerations: The nature and type of product have an important bearing on the choice of distribution channels. For examples, perishable goods need speedy movements and hence shorter channel or route of distribution; For durable goods, longer and diversified channels may be used; Similarly, for technical products requiring specialised selling and serving talents, the shortest channel should be used.

(b) Market considerations: The nature and type of customers and size of market are important considerations in the choice of a channel of distribution.

For example, if the market size is large, there may be long channels, whereas in a small market direct selling may be profitable. The nature and type of consumers include factors such as desire for credit, preference for the stop shopping, demand for personal services, amount of time and effort the customer is willing to spend. It also includes factors like age, income group, sex, and religion of customers.

(c) Company considerations: The nature, size and objectives of the business firm also play an important role in the selection of distribution channel. It includes financial resources, market standing, volume of production, desire for control of channel, services provided by manufacturers', etc. For example a company with substantial financial resources need not rely too much on the middlemen and can afford to reduce the levels of distribution. Similarly a company desiring to exercise greater control over channel will prefer a shorter channel.

(d) Middlemen considerations: The cost and efficiency of distribution depend largely on the nature and type of middlemen. It includes characteristics of middlemen such as availability, attitudes, services, sales potential, costs etc. For example, if the terms and conditions of engaging wholesalers are unfavourable, a manufacturer may like to channelise his products through semi-wholesalers or retailers, thereby, bypassing wholesalers. However, the determining factor would be the differential advantage involved in the choice.

To conclude, the channel generating the largest sales volume at lower unit cost will be given top priority. This will minimise distribution cost.

Q9. Explain briefly role of middleman. [June 2006, Q1(d)]

Ans. Role of middlemen in the distribution of goods: The middlemen perform the following marketing functions which are listed in sequence.

(a) Searching out buyers and sellers (contacting & Mechandising), matching goods to the requirements of market.

(b) Offering goods in the form of assortments or packages.

(c) Persuading and influencing the prospective buyers to favour a certain product and its maker (personal selling/sales promotion).

(d) Implementing pricing policies in such a manner that would be acceptable to buyers and ensure effective distribution.

(e) Providing feed back information, marketing intelligence and sales forecasting services for the regions to their suppliers.

(f) Looking after the process of distribution where necessary.

(g) Participating actively in the creation and establishment of a market for a new product.

(h) Offering pre and after sale services to consumers.

(i) Communicating the use of technique of the product to the users.

(j) Offering credit to retailers and consumers.

(k) Risk bearing with reference to stock hoarding/transport.

Q10. Who is Wholesalers? Describe the types and functions of wholesalers. [June 2008, Q1(c)] [June 2005, Q4]

Ans. Role of Wholesaler : Wholesaler acts as a middlemen in the channel of distribution as he buys goods in large quantity from the manufacturer and sells these to retailers in small quantities. His role in distribution of goods is discussed below :

(a) **Buying and assembling:** A wholesaler forecasts the demand for goods and assembles different varieties of goods from several manufacturers. Some wholesalers also import goods from foreign countries.

(b) **Selling and dispersing:** A wholesaler breaks the bulk so that retailers and users can buy them in small lots. His representatives regularly call on retailers and industrial users/buyers to distribute the goods among widely scattered people.

(c) **Transportation:** A wholesaler arranges transportation of goods from producers to his godowns and from there to retailers. Sometimes he has his own transport arrangement for this purpose.

(d) **Storage:** He holds large stocks and serves as a reservoir and supplies to retailers. He helps in stablising prices by adjusting supply of goods to their demand.

(e) **Packing and grading:** A wholesaler packs and repacks goods in convenient lots. He sorts out goods in different grades. He also gives brand names to the products packed and graded by him.

(f) **Advertising and sales promotion:** A wholesaler performs advertising and sales promotion activities to increase the sale of products. He also takes the services of experts for this purpose.

(g) **Financing:** Sometimes the wholesaler buys goods on cash basis from manufacturers and sells them on credit to retailers. In this way he provides financial help both to the producers and retailers. If necessary, the wholesaler also provide financial help by way of advance payment to producers.

(h) **Risk-taking:** A wholesaler bears risks of changes in demand and prices, bad debts and damage to goods in the course of transportation and storage. By undertaking various risks he simplifies the process of distribution.

Q11. What are the services rendered by a retailer to consumer?

Ans. Retailers deal with wholesales and consumers. Manufacturers as well as wholesalers depend a great deal on retailers for reaching the ultimate consumers to supply various products. Retailers provide the necessary outlet for goods and thus render very useful service to the wholesalers and also to the producers indirectly. The services of retailers to the customers are significant in several ways:

(a) Holding ready stocks : By holding stocks, retailers supply varieties of goods of daily use to consumers. Besides, consumers are also given opportunity to make their choice from several varieties produced by different firms.

(b) Display of goods : By displaying goods on shelves or in show-cases, retailers bring new products to the notice of customers. They also keep the customers informed about the latest varieties of goods available for sale by explaining their qualities and prices. Customers are also given demonstration of new products on the sales counter.

(c) Advice to consumers : Very often retailers help the customers to make their decision to buy certain goods by advising them on the merits and use of particular varieties of products.

(d) Personal services : Apart from meeting the needs of different types of customers, retailers also offer a variety of services like home delivery, sale on credit, etc.

Q12. What are the functions performed by retailers?

[June 2008, Q1(c)]

Ans. Role of Retailers: Retailers buys goods from wholesaler and sells them directly to consumers. Thus he acts as a direct link between the wholesaler and consumers. His role in distribution of goods is enumerated below:

(a) Wide choice to consumers: The retailer anticipates needs of consumers. He assembles goods from different sources and stocks different varieties of products. Thus, he offers a wide choice to consumers. They can buy according to their purchasing power and requirements.

(b) Availability of goods in small quantities and at convenient locations: A retailer provides ready supply of goods so that consumers can buy conveniently and quickly in small lots without any inconvenience of placing advance orders and waiting for supplies. By ensuring uninterrupted and fresh supply of goods, he saves consumers from the botheration of buying goods in bulk and storing them.

(c) Home delivery: A retailer transports goods from wholesalers to ultimate consumers. Some retailers provide free home delivery service to their consumers. Thus they create place utility.

(d) Assurance of regular supply: He maintains adequate supply of goods so that consumers are sure of getting regular supply at the time of their need.

(e) Credit facility: Although retailers mostly sell goods for cash, they also supply goods on credit to their regular customers.

(f) Close interaction with customers: A retailer brings new products to the notice of customers and educates them in their uses. A retailer thus, acts as a friend and guide to his customers. Indeed his interaction with customers is of intimate personal nature and thus he is able to provide feed back to wholesalers and manufacturers about consumers' preferences.

Q13. Discuss briefly:
(1) Departmental house
(2) Mail-order house
(3) Super-market

Ans. (1) Departmental store: A **department store** is a retail establishment which specializes in selling a wide range of products without a single predominant merchandise line. Department stores usually sell products including apparel, furniture, appliances, electronics, and additionally select other lines of products such as paint, hardware, toiletries, cosmetics, photographic equipment, jewelery, toys, and sporting goods. Certain department stores are further classified as discount department stores. Discount department stores commonly have central customer checkout areas, generally in the front area of the store. Department stores are usually part of a retail chain of many stores situated around a country or several countries.

Types of Department Stores:

Upscale Department Store : Characteristics of a typical upscale department store may include:

- **(a)** Sale of brand name perfumes and beauty supplies, like Burberry, Calvin Klein or MAC at the main entrance, with specialists in cosmetics there to assist customers with applying and selecting makeup.
- **(b)** General sale of name brand clothes above an average price level, such as Dior, Chanel, Versace, Lacoste, etc.
- **(c)** When items are discounted, the price resembles that of an average priced item at a lower scale department store.
- **(d)** Sale of small household appliances like blenders, or small electronic items such as portable radios.
- **(e)** Specialized services or subset businesses such as personal shopping assistance, salons, restaurants, and/or travel agencies.

Some upscale department stores that operate in the United States include national chains like Barneys New York, Bloomingdale's, Lord & Taylor, Neiman Marcus, Nordstrom, and Saks Fifth Avenue, as well as regional retailers such as Bergdorf Goodman, and Von Maur. In the United Kingdom, department stores making up the high-end include Harvey Nichols, Harrods and Fortnum and Mason. In Indonesia, the most upscale department stores includes Sogo and Seibu from Japan, Debenhams and Harvey Nichols from United Kingdom (all managed by PT. Mitra Adiperkasa Tbk.), and Parisian from Indonesia (managed by Lippo Group).

Mid-Scale Department Stores: Depending upon location, Belk, Dillard's and Macy's, are sometimes considered upscale department stores, but the chains overall are often viewed as being situated somewhere between midscale and higher midscale.

Mid-Range Department Store: Characteristics of a mid-range department store may include:

(a) Sale of cosmetics.
(b) Sale of some brand names, with greater emphasis on private label brands.
(c) Sale of accessories.
(d) Sale of some small household appliances.
(e) Sale of furniture in larger locations.

Comparison to Upscale Department Store :

(a) Sale of cosmetics but generally not brand name. Fragrances and beauty supplies may be placed further into the interior of the store, without cosmetic specialists at the counters.
(b) Greater proportion of moderately-priced brand names.
(c) Accessories and purses aren't upscale brand names, with greater proportion of lesser-known or private label branded items.

Mid-range department stores that operate in the United States include national chains JCPenney and Kohl's. Regional chains such as Gottschalks and Mervyns in the western United States, and The Bon-Ton and associated stores in the northern part of the country are also among this grouping of stores.

As noted in details of upscale department stores, Macy's, Dillard's and Belk vary in price points and relative consideration as upscale or mid-range versus local competitors, depending upon location. Some larger locations in affluent areas often carry significant selections of brand name products including brand name accessories and fragrances kept in glass cases, and usually have cosmetic specialists in the beauty department. Brands at above-average price points, if offered at all, are generally limited and full product lines of such brands are not typically available. Smaller and more remote store locations – often, the legacy of acquisitions of smaller retailers – may concentrate squarely on moderately-priced merchandise. California-based Gottschalks mirrors these chains, though in a specific region with little presence in major metropolitan areas. Macy's are typically the anchors of upscale malls and are situated among other high-end department stores such as Tysons Galleria or The Domain in Austin. Nationally known JCPenney has incorporated elements of upscale stores such as salons and custom home decorating services, along with offering optical shops, portrait photography studios and designer-produced private labels.

The national chain Sears is also in this category, but often is considered a lower grade mid-range department store due to marketing a higher proportion of private label and lesser-known label goods in apparel and housewares segments. Sears differs from most mid-range department store chains in its common inclusion of departments for hardware, garden and outdoor equipment, automotive service, and large appliances and electronics – product segments more typical of discount or so-called "big box" retailers.

Discount Department Store/Super-Store :

(a) Sells cosmetics, generally not name brand.
(b) Generally doesn't sell name brands.
(c) Sells accessories, generally not name brand.
(d) Sells small household appliances.
(e) Sells toys, electronics and video games.
(f) Sells household necessities.
(g) The "super-store" variant usually sells food products and has a "one stop shop" vibe.

Comparison to Mid-Range Department Stores :

(a) Sells fewer major brand names.
(b) Offers a wider variety of products.
(c) More likely to anchor a power centre than an indoor shopping mall.

Some discount department stores that operate in the United States include: ShopKo, Kmart and Wal-Mart. Although ShopKo and Kmart are more upscale than Wal-Mart; further, Wal-Mart could be considered a "super discount department store". Target is also in this category but may be considered a more upscale Discount Department Store because it puts a greater emphasis on current fashion and on special merchandise lines from well-known designers such as Isaac Mizrahi and Thomas O'Brien.

Off-Price Retailer :

(a) Most products are name-branded.
(b) Products may be over-runs, seconds, or last season's stock liquidated from department stores.
(c) Product mix typically emphasizes women's clothing and may include men's clothing, children's clothing, shoes, accessories, perfume, toys, housewares, or packaged gourmet food.
(d) Stores are most frequently located in power centres but may also appear in shopping malls.

Off-price retail department stores include T.J. Maxx, Factory 2-U, Century 21, Gabriel Brothers, Ross Dress For Less, Marshalls, and Burlington Coat Factory. TJX, the parent company of Marshall's, and TJ Maxx, has been experimenting with Home Goods superstores that carry a larger range and variety of housewares, including furniture.

(2) Mail-order House: Retail trading which consists of receiving orders by mail and delivery of goods by parcel post is known as mail order business. The mail-order house is thus a retail trading organization which uses the post office as its channel of distribution. Standard consumer goods with trade marks or brand names are generally dealt with by mail order houses. This is because customers are to place orders without physically checking the items. Bulky goods which cannot be delivered by post and those for which delivery costs are relatively higher, are not included in the items traded. Orders from customers may be secured by advertising in newspapers or journals. Sometimes circular letters are issued by mail to certain categories of customers. For this purpose, a mailing list may be prepared from the telephone directory or from the list of members of a club or traders' association. The mailing list contains the names and addresses of persons likely to be interested in the particular goods. Customers are invited to send their orders by post to the address of the mail order house. Delivery is made by V.P.P. (Value Payable Post). Goods are thus available to the customers on payment of the price which is remitted by the post office to the sender of goods.

Mail-order business helps customers to get their requirements at their own place and save the time and expense of shopping. The mail-order house, on the other hand, is also benefited in a number of ways. Goods can be procured according to the orders received. The business can thus be started with a small amount of capital. Payment for goods is assured through the post office. A wide market can be covered by means of postal communication. However, mail order business has not developed in India mainly due to the existence of retail trading shops in every locality. Besides, illiterate people cannot be approached through the mailing list.

(3) Super-markets : A **supermarket** is a self-service store offering a wide variety of food and household merchandise, organized into departments. It is larger in size and has a wider selection than a traditional grocery store and it is smaller than a hypermarket or superstore. The supermarket typically comprises meat, fresh produce, dairy, and baked goods departments along with shelf space reserved for canned and packaged goods as well as for various nonfood items such as household cleaners, pharmacy products, and pet supplies. Most supermarkets also sell a variety of other household products that are consumed regularly, such as alcohol (where permitted), household cleaning products, medicine, clothes, and some sell a much wider range of nonfood products.

The traditional suburban supermarket occupies a large amount of floor space, usually on a single level, and is situated near a residential area in order to be convenient to consumers. Its basic appeal is the availability of a broad selection of goods under a single roof at relatively low prices. Other advantages include ease of parking and, frequently, the convenience of shopping hours that extend far into the evening or even 24 hours a day. Supermarkets usually make massive outlays of newspaper and other advertising and often present elaborate in-store displays of products. The stores often are part of a corporate chain that owns or controls (sometimes by franchise) other supermarkets located nearby – even transnationally – thus increasing opportunities for economies of scale.

In North America, supermarkets typically are supplied by the distribution centers of its parent company, such as Loblaw Companies in Canada, which operates thousands of supermarkets across the nation. Loblaw operates a distribution center in every province – usually in the largest city in the province.

Supermarkets usually offer products at low prices by reducing their economic margins. Certain products (typically staple foods such as bread, milk and sugar) are occasionally sold as loss leaders, that is, with negative profit margins. To maintain a profit, supermarkets attempt to make up for the lower margins by a higher overall volume of sales, and with the sale of higher-margin items. Customers usually shop by placing their selected merchandise into shopping carts (trolleys) or baskets (self-service) and pay for the merchandise at the check-out. At present, many supermarket chains are attempting to further reduce labor costs by shifting to self-service check-out machines, where a single employee can oversee a group of four or five machines at once, assisting multiple customers at a time.

A larger full-service supermarket combined with a department store is sometimes known as a hypermarket. Other services offered at some supermarkets may include those of banks, cafes, childcare centers/creches, photo processing, video rentals, pharmacies, and/or gas stations.

Supermarkets use stock rotation, the practice of moving products with an earlier sell-by date to the front of a shelf so they get picked up and sold first.

Q14. What is Foreign Trade? Discuss the types and importance of foreign trade. [Dec 2007, Q2(c)]

Ans. Nations, like individuals, do not possess everything they need to fulfill their requirements. Even countries like the USA and China, which are rich in natural and human resources have to look to other countries for supply of some of their requirements. For instance, consumers in USA obtain their supply of sugar and coffee from other countries. Moreover, different countries possess different types of resources. Those which have a surplus of certain resources find it beneficial to sell the surplus items to some other countries and buy other items which they need. Such exchange of goods and services between people across national boundaries is called 'foreign trade' or 'international trade'. Foreign trade can be bilateral or multilateral. When there is trade between people of any two nations, it is **bilateral**: foreign trade is **multilateral** when people of any country buy from and sell to people of more than one country.

The difference between home trade and foreign trade is that while home trade takes place within a country among people who are citizens of that country, the foreign trade takes place beyond the national boundaries of two or more countries. Besides this, there are other differences which may be stated as follows:

(i) There is little restriction on trade between people within a country. But in case of foreign trade the restrictions are numerous. A firm requires permission from Government authorities before goods can be imported or exported.

(ii) In domestic trade payment made by the buyer and received by the seller of goods is in the same units of money. In foreign trade, what the importer pays in his national currency has to be converted into foreign currency acceptable to the exporter.

(iii) Payment can be made either in cash or by cheque on a national bank in the case of home trade. Payment can be made only through bank in the case of foreign trade.

Types of Foreign Trade: Foreign trade can be divided into three categories. They are :

(i) Import Trade

(ii) Export Trade, and

(iii) Entrepot Trade

When goods are sold to a trader in any foreign country, they are said to be exported to that country and it is known as **'export trade'**. When purchases are made from a foreign country, goods are said to be imported into the country and it is called **import trade**. Many a time goods are imported from one country with the objective of exporting them to some other country or countries. This is known as **entrepot trade**. City states like Singapore and Hong Kong are important entrepot trade centres.

Importance of Foreign Trade : Production of goods and services requires different resources like men, materials, money, machines and management. If we compare the resources possessed by nations it will be found that no country is self-sufficient and there are difference in the quality and quantity of domestic resources available in different countries. Indeed, it is this difference in the relative abundance or shortage of resources in different countries that has given rise to foreign trade involving exchange of goods and services between countries. Through international trade, it is possible to avail of goods which it cannot produce or cannot produce as economically as other countries. Hence, a country's well-being is determined to a great extent by the nature and extent of its foreign trade. Let us discuss the importance of foreign trade to people in different countries.

(a) Specialisation and efficiency of production: Foreign trade leads to specialization in productive activities undertaken by different countries. Depending on available natural resources and development of science and technology, every country can produce only those goods and services for which it has the greatest relative advantage and efficiency. No country has facility and resources within its own boundaries for economical production of all its requirements. Some countries are more suitably placed to produce certain goods/services economically and sufficiently than other countries. Therefore, they can specialise in the production of such goods and get the goods they need in exchange for those goods. For example, India has comparatively greater advantages for the production of agrobased products such as coffee, tea, sugar, textiles, etc. Similarly some developed countries such as USA, Japan, Britain, etc. have greater advantages for the production of industrial machinery, automobiles, etc. Some gulf countries such as Iran, Libya, Saudi Arabia, etc. produce crude oil, petroleum, etc. in abundance.

(b) Utilisation of resources: Every country possesses some natural resources. The economic development of a country heavily depends upon exploitation of these resources. For example, India has adequate off-shore oil resources. But, it requires exploitation through sophisticated machines, technology, etc. which we do not have. Machinery and technology can be imported from the developed countries like USSR, USA, Japan, etc. This leads to best possible use of natural resources.

(c) Facilitates economic development: Rapid economic development and growth of national income can be facilitated on the basis of exports and imports. Indeed, it is on the basis of imports of raw materials and export of manufactured goods that countries like U.K., Japan etc. have achieved a high rate of economic growth.

(d) Equalisation of prices: International trade equalizes prices of goods throughout the world. Whenever the prices of commodities tend to rise in a country, it can increase the level of its imports to check the rise in prices. Similarly, whenever prices of products decline, the trend may be counteracted by exporting the same.

(e) Employment opportunities: Foreign trade facilitates the growth of agricultural as well as industrial activities which in turn generates more employment in the country.

(f) Harmonious relationship between countries: Because of foreign trade every country may have access to goods that it does not produce at home. Similarly, a country with a surplus of certain goods can make them available to other countries experiencing shortage of those goods. This promotes harmonious and cordial relationship among various countries.

Q15. Discuss about the problems relating to foreign trade.

Ans. Foreign trade has to face certain problems because of cultural, geographical and other environmental differences between various countries. These problems are:

(1) Product: The very first thing a foreign marketer has to see whether the product offered is suitable for the foreign market. Securing information about this requires a lot of skills and expenditure.

(2) Demand and Supply Conditions: Entry of local and international competitors and changes in buyer's preference can change the balance of demand and supply in a foreign market, which is not easily accessible.

(3) Price Changes: The price of products in international markets are affected by lot of factors like import, export duties, exchange rates of currencies etc. These prices keep on changing frequently. A foreign trade has to cope up with this problem.

(4) Credit Risk: International trade is done on a large scale and on credit. A marketer has to bear the risk of arising from the buyer's default, bankruptcy etc.

(5) Rules and Regulations: In foreign trade rules and regulations of trade differ from country to country. Besides, every country imposes certain restrictions to protect its economic and political interest. Sometimes these practices create problems for international traders.

(6) Transportation and Cargo Risk: In international trade goods are moved over long distances. In spite of all developments in transportation, the risks of loss or damage to cargo by fire, storm, explosion, spoilage etc. exist.

(7) Time Gap: In international trade, distance is longer, hence transit time is also longer. This time gap involves exporter's capital being blocked up over a long period.

In pre-independence period, India's foreign trade was confined to exports of traditional items. Products like foodstuffs, raw cotton, tea, spices, tobacco consisted 85% of the total exports. The import consisted of consumer goods and manufactured products. The major part of India's foreign trade was confined to Britain as its colony.

After independence, India saw a radical change in foreign trade. The major export shifted to gems and jewellery, readymade garments, agro-based products, chemicals, machinery and metal products etc. The market for foreign trade consists of countries like U.S.A., Japan, Germany, U.K. and other countries of all economies, developed, underdeveloped and developing.

Table given below shows the growth of foreign trade since 1950-1951:

Year	**Export**	**Imports**	**Balance of Trade**
1950-51	606	608	–2
1960-61	642	1122	–480
1970-71	1535	1634	–99
1980-81	6711	12549	–5838
1990-91	32553	43198	–10645
1995-96	74493	86064	–11571
(April-Dec) Provisional			

Q16. Which steps are involved in the general procedure of import trade in India? [Dec 2006, Q4]

Ans. Import trade procedure differs from country to country depending upon the satisfactory requirements and trade practices in force. The general procedure of import trade in India involves the following stages:

(1) Trade Enquiry
(2) Obtains an Import Licence
(3) Obtains Foreign Exchange
(4) Places the Order/Indent
(5) Arranges Letter of Credit
(6) Gets Shipping Documents
(7) Clears the Goods
(8) Makes Payments

(1) Trade Enquiry: The intending importer makes trade enquiry from the possible exporters. His enquiry is based on the details of the goods required by him viz., quality, design, size, etc. and seeks information regarding the availability of goods, the price at which they would be available and the terms and conditions regarding delivery and payment. In response to his enquiry, the importer may receive a number of quotations, which will contain particulars as of the goods available in ready stock, their quality, size, design etc. The different quotations will also specify the price at which the goods should be available and the terms and conditions of sale. Once quotations from different suppliers have been received, a thorough comparison should be made of the various quotations before taking the decision to import.

(2) Obtain an Import Licence: In order to obtain an import licence, the intending importer makes an application in the prescribed form, to the Licencing Authority. When the licencing authority is satisfied with the claims, he issues the licence. The import licence is issued in duplicate. The first copy is presented by the importer to the customs authority at the time of clearance of goods and the second copy is used for obtaining foreign exchange from Reserve Bank of India. Although raw materials, intermediates, capital goods and other items announced by the central government may be imported freely under Open General Licence (OGL) scheme.

(3) Obtains Foreign Exchange: After obtaining the import licence, the importer makes arrangements for obtaining the necessary amount of foreign currency. In India, the Reserve Bank of India (RBI) is authorised by the Government to regulate the use of exchange. Every importer has to produce import licence along with the prescribed application form under the Exchange Control Act. The exchange bank of the importer endorses and forwards the application to the Exchange Control Department of RBI. The RBI sanctions the release of the amount of foreign exchange to the importer after scrutinising the application on the basis of the existing Government policy.

(4) Places the Order/Indent: After obtaining the import licence and requisite amount of foreign exchange, the next step is to place the order or indent for import of the goods. An indent is a form of order sent abroad for goods to be imported. The indent contains full details regarding the goods to be imported and the terms and conditions regarding price, shipment, delivery, the method of payment etc. An indent may be 'open', 'closed' or 'confirmatory'. When the selection of goods and other details are left to the agent's discretion in the foreign country, it is called an **'open indent'**. A **closed indent** contains full particulars of the exact goods required. When an order is placed subject to the confirmation by the importer's agent, it is called **confirmatory indent**. Every importer is free to place the order directly or through the intermediaries, specialised in such trade. These specialised agencies are called **indent house**. An indent house refers to an import agent or import firm, which imports goods on orders received from importers. The indent house serves as middlemen between the importers and exporters. They charge certain percentage of commission for their services from the importer. If the importer wants to make use of services of an indent house, he has to enter into an agreement with the indent house for the supply of specified goods. For this purpose there are certain special forms which the indent house fills up and the importer signs. In India many of the big indent houses have their offices in port towns like Bombay, Madras, Calcutta etc.

(5) Arranges Letter of Credit: Depending upon the terms of payment, the importer may have to arrange a letter of credit to be issued by his bank in favour of the exporter. All the terms and conditions agreed upon between the importer and exporter are generally spelt out in the letter of credit. The importer's bank issues the letter of credit authorising the correspondent bank in the exporter's country to buy the bill drawn by the exporter on the importer or to accept the bill drawn on the bank itself. The importer's bank may require adequate amount to be deposited by the importer so as to cover the amount for which the letter of credit is issued. But such a deposit may not be insisted upon if the importer is an established person or a firm well known to the bank or it maintains a satisfactory deposit account with the bank.

A bank may issue any of the following types of letter of credit:

(a) **Revocable letter of credit:** It can be withdrawn or altered or revoked at the discretion of the issuing bank without the prior consent of the exporter.

(b) **Unconfirmed irrevocable letters of credit:** It cannot be cancelled or altered or withdrawn by the issuing bank prior to the date of expiry, without the consent of the exporter and is thus much safer.

(c) **Confirmed irrevocable letters of credit:** The irrevocable letter of credit shall be more safe it is confirmed or guaranteed by a bank. With a confirmed irrevocable credit, the bank must pay the exporter, whatever happens to the importer or the foreign bank.

(6) Gets Shipping Documents : After receiving order and the letter of credit, the exporter ships the goods and intimates the importer that the goods have been despatched. The exporter draws a bill of exchange on the importer's bank for the full value of goods payable to him. The bill of exchange, accompanied by all the shipping documents viz. commercial invoice, bill of lading, insurance policy and the certificate of origin are forwarded to the importer's bank by the exporter's bank. Under the letter of credit arrangement, the importer's bank will handover the documents to the importer who would take steps for getting the goods cleared from the customs authorities. In the absence of a letter of credit, the bank will follow the instructions of the exporter in the matter of delivering the documents to the importer. If the bill of exchange is marked D/A, the documents will be delivered to the importer on the acceptance of the bill. If the bill is marked D/P, the documents will be delivered to the importer only on payment of the amount of the bill.

(7) Clear the Goods: After taking possession of the documents of title to the goods, the importer waits for the arrival of the ship. When the ship arrives at the port of destination, the importer arranges clearance of the goods from the customs office in whose custody the goods lie after being unloaded from the ship. This requires a number of formalities to be completed. The importer may appoint a clearing agent for that purpose. Clearance of goods requires the following steps to be taken: (i) get the bill of lading endorsed by the shipping company for delivery of the goods or a delivery order issued by the shipping company (ii) pay the necessary amount of port trust dues representing the cost of services rendered by the dock authorities in connection with the loading of goods (iii) fill up a 'bill of entry' containing all particulars relating to the imported goods and the customs duty to be paid. After import duty has been paid, the importer has to submit the 'bill of lading' 'port trust dues receipt' and 'bill of entry' to the shipping company for release of the goods. In case the importer is not in a position to pay the customs duty in full immediately, he may apply to the customs authorities to get them placed in the **bonded warehouse**. The importer can pay duty for part of the goods as and when he wants to get delivery.

(8) Makes Payments: The mode of payment for import depends upon the agreement between the importer and the exporter. If the documents have been received against acceptance, the importer has to honour the bill of exchange on the due date. After the bill is paid, the importer transaction comes to a close. In case of documents against payment, the importer pays immediately or within a short period after presentation, because the importer gets possession of the documents of title to the goods only on payment of the bill.

Q17. Distinguish between :
(1) Bill of lading and shipping bill **[June 2003, Q3(a)]**
(2) Bill of lading and charter party
(3) Mate's receipt and shipping order.

Ans. (1) Bill of lading and shipping bill : A **bill of lading** (sometimes referred to as a **BOL, or B/L**) is a document issued by a carrier, e.g. a ship's master or by a company's shipping department, acknowledging that specified goods have been received on board as cargo for conveyance to a named place for delivery to the consignee who is usually identified. A *through* bill of lading involves the use of at least two different modes of transport from road, rail, air, and sea. The term derives from the noun "bill", a schedule of costs for services supplied or to be supplied, and from the verb "to lade" which means to load a cargo onto a ship or other form of transport.

It is quite evident that bill of lading can be used as a traded object. The standard short form bill of lading is evidence of the contract of carriage of goods and it serves a number of purposes:

(a) It is evidence that a valid contract of carriage, or a chartering contract, exists, and it may incorporate the full terms of the contract between the consignor and the carrier by reference (i.e. the short form simply refers to the main contract as an existing document, whereas the long form of a bill of lading (*connaissement intégral*) issued by the carrier sets out all the terms of the contract of carriage);

(b) It is a receipt signed by the carrier confirming whether goods matching the contract description have been received in good condition (a bill will be described as *clean* if the goods have been received on board in apparent good condition and stowed ready for transport); and

(c) It is also a document of transfer, being freely transferable but not a negotiable instrument in the legal sense, i.e. it governs all the legal aspects of physical carriage, and, like a cheque or other negotiable instrument, it may be endorsed affecting ownership of the goods actually being carried. This matches everyday experience in that the contract a person might make with a commercial carrier like FedEx for mostly airway parcels, is separate from any contract for the sale of the goods to be carried, however it binds the carrier to its terms, irrespectively of who the actual holder of the B/L, and owner of the goods, may be at a specific moment.

(2) Bill of lading and charter party: (see previous question for bill of lading)

Charter party- Charter Party (Lat. charta partita, a legal paper or instrument, divided, i.e. written in duplicate so that each party retains half), a written, or partly written and partly printed, contract between a shipowner and a merchant, by which a ship is let or hired for the conveyance of goods on a specified voyage, or for a defined period. A vessel might also be chartered to carry passengers on a journey. Also, a written contract between shipowner and charterer whereby a ship is hired; all terms, conditions and exceptions are stated in the contract or incorporated by reference.

A charter party is the contract between the owner of a vessel and the charterer for the use of a vessel. The charterer takes over the vessel for either a certain amount of time (a time charter) or for a certain point-to-point voyage (a voyage charter), giving rise to these two main types of charter agreement. There is a subtype of time charter called the demise or bareboat charter.

In a time charter, the vessel is hired for a specific amount of time. The owner still manages the vessel but the charterer givers orders for the employment of the vessel, and may sub-charter the vessel on a time charter or voyage charter basis. The demise or bareboat charter is a subtype of time charter in which the charter takes responsibility for the crewing and maintenance of the ship during the time of the charter, assuming the legal responsibilities of the owner and is known as a disponent owner.

In a voyage charter, the charterer hires the vessel for a single voyage, and the vessel's owner (or disponent owner) provides the master, crew, bunkers and supplies.

(3) Mate's receipt and shipping order: Mate's receipt is a receipt issued by the Commanding Officer of the ship when the cargo is loaded on the ship. The mate's receipt is a prima fade evidence that the goods are loaded in the vessel. The mate's receipt is first handed over to the f Port Trust Authorities. After making payment of all port dues, the exporter or his agent collects the mate's receipt from the Port Trust Authorities. The mate's, receipt is freely transferable. It must be handed over to the shipping company in order to get the' bill of lading. Bill of lading is prepared on the basis of the mate's receipt.

Types of Mate's Receipts:

(a) Clean Mate's Receipt: The Commanding Officer of the ship issues a clean mate's receipt; if he is satisfied that the goods are .packed properly and there is no defect in the packing of the cargo or package.

(b) Qualified Mate's Receipt: The Commanding Officer of the ship issues a qualified mate's receipt, when the goods are not packed properly and the shipping company does not take any responsibility of damage to the goods during transit.

Contents of Mate's Receipt :

(a) Name and logo of the shipping line.
(b) Name and address of the shipper.
(c) Name and the number of vessel.
(d) Name of the port of loading.
(e) Name of the port of discharge and place of delivery.
(f) Marks and container number.
(g) Packing and Container description.
(h) Total number of containers and packages.
(i) Description of goods in terms of quantity.
(j) Container status and seal number.
(k) Gross weight in kg. and volume in terms of cubic meters.
(l) Shipping bill number and date.
(m) Signature and initials of the Chief Officer.

Significance of Mate's Receipt :

(a) It is an acknowledgement of goods received for export on board the ship.

(b) It is a transferable document. It must be handed over to the shipping company in order to get the bill of lading.

(c) Bill of lading, which is the title of goods, is prepared on the basis of the mate's receipt.

(d) It enables the exporter to clear port trust dues to the Port Trust Authorities.

Shipping order: Inventory control document that is used to identify what should be shipped from the warehouse and to whom and where it should be shipped. The shipping order usually accompanies the shipment, so that the recipient can verify that the items listed were received. The shipping order can then be used to prepare an invoice or, in the case of a collect on delivery (cod) order, can serve as the invoice. The information included on a shipping order is typically an order number and date, shipping and receipt dates, a customer purchase order number, special shipping instructions such as "UPS" or "overnight," the buyer's name and address, the shipping address (if different), and a list of the items ordered, shipped, and/or back-ordered, including quantity and warehouse storage location. The shipping order may also include a space for the recipient's signature.

Chapter-4

Business Services

Q1. What is Bank? Discuss the types of bank.

Ans. A **banker** or **bank** is a financial institution whose primary activity is to act as a payment agent for customers and to borrow and lend money. It is an institution for receiving, keeping, and lending money.

The first modern bank was founded in Italy in Genoa in 1406, its name was *Banco di San Giorgio* (Bank of St. George).

Many other financial activities were added over time. For example banks are important players in financial markets and offer financial services such as investment funds. In some countries such as Germany, banks are the primary owners of industrial corporations while in other countries such as the United States banks are prohibited from owning non-financial companies. In Japan, banks are usually the nexus of cross share holding entity known as zaibatsu. In France "Bancassurance" is highly present, as most banks offer insurance services (and now real estate services) to their clients. Following are the types of bank :-

Types of banks: Banks' activities can be divided into retail banking, dealing directly with individuals and small businesses; business banking, providing services to mid-market business; corporate banking, directed at large business entities; private banking, providing wealth management services to high net worth individuals and families; and investment banking, relating to activities on the financial markets. Most banks are profit-making, private enterprises. However, some are owned by government, or are non-profits.

Central banks are normally government owned banks, often charged with quasi-regulatory responsibilities, e.g. supervising commercial banks, or controlling the cash interest rate. They generally provide liquidity to the banking system and act as the lender of last resort in event of a crisis.

Types of retail banks:

(a) Commercial bank: The term used for a normal bank to distinguish it from an investment bank. After the Great Depression, the U.S. Congress required that banks only engage in banking activities, whereas investment banks were limited to capital market activities. Since the two no longer have to be under separate ownership, some use the term "commercial bank" to refer to a bank or a division of a bank that mostly deals with deposits and loans from corporations or large businesses.

(b) Community Banks: Locally operated financial institutions that empower employees to make local decisions to serve their customers and the partners

(c) Community development banks: Regulated banks that provide financial services and credit to under-served markets or populations.

(d) Postal savings banks: Savings banks associated with national postal systems.

(e) Private banks: Manage the assets of high net worth individuals.

(f) Offshore banks: Banks located in jurisdictions with low taxation and regulation. Many offshore banks are essentially private banks.

(g) Savings bank: In Europe, savings banks take their roots in the 19th or sometimes even 18th century. Their original objective was to provide easily accessible savings products to all strata of the population. In some countries, savings banks were created on public initiative, while in others socially committed individuals created foundations to put in place the necessary infrastructure. Nowadays, European savings banks have kept their focus on retail banking: payments, savings products, credits and insurances for individuals or small and medium-sized enterprises. Apart from this retail focus, they also differ from commercial banks by their broadly decentralised distribution network, providing local and regional outreach and by their socially responsible approach to business and society.

(h) Building societies and Landesbanks: Conduct retail banking.

(i) Ethical banks: Banks that prioritize the transparency of all operations and make only what they consider to be socially-responsible investments.

(j) Islamic banks: Banks that transact according to Islamic principles.

Types of investment banks :

(a) Investment banks “underwrite” (guarantee the sale of) stock and bond issues, trade for their own accounts, make markets, and advise corporations on capital markets activities such as mergers and acquisitions.

(b) Merchant banks were traditionally banks which engaged in trade finance. The modern definition, however, refers to banks which provide capital to firms in the form of shares rather than loans. Unlike venture capital firms, they tend not to invest in new companies.

Both combined : Universal banks, more commonly known as financial services companies, engage in several of these activities. For example, First Bank (a very large bank) is involved in commercial and retail lending, and its subsidiaries in tax-havens offer offshore banking services to customers in other countries. Other large financial institutions are similarly diversified and engage in multiple activities. In Europe and Asia, big banks are very diversified groups that, among other services, also distribute insurance, hence the term bancassurance is the term used to describe the sale of insurance products in a bank. The word is a combination of "banque or bank" and "assurance" signifying that both banking and insurance are provided by the same corporate entity.

Other types of banks:

Islamic banking : Islamic banks adhere to the concepts of Islamic law. Islamic banking revolves around several well established concepts which are based on Islamic canons. Since the concept of interest is forbidden in Islam, all banking activities must avoid interest. Instead of interest, the bank earns profit (mark-up) and fees on financing facilities that it extends to the customers.

Q2. Explain briefly the functions of a modern commercial bank. [Dec 2008, Q1(c)]

Ans. Commercial Bank: Bank that makes loans to businesses, consumers, and nonbusiness institutions. Early commercial banks were limited to accepting deposits of money or valuables for safekeeping and verifying coinage or exchanging one jurisdiction's coins for another's. By the 17th century most of the essentials of modern banking, including foreign exchange, the payment of interest, and the granting of loans, were in place. It became common for individuals and firms to exchange funds through bankers with a written draft, the precursor to the modern check. Because a commercial bank is required to hold only a fraction of its deposits as cash reserves, it can use some of the money deposited by its customers to extend loans. Commercial banks also offer a range of other services, including savings accounts, safe-deposit boxes, and trust services.

Functions of Commercial Banks: The functions of the commercial banks are divided into two categories:

(1) Primary functions, and

(2) Secondary functions including agency functions.

(1) Primary functions : The primary functions of a commercial bank include :

(a) Accepting deposits : The most important activity of a commercial bank is to mobilise deposits from the public. People who have surplus income and savings find it convenient to deposit the amounts with banks. Depending upon the nature of deposits, funds deposited with bank also earn interest. Thus, deposits with the bank grow along with the interest earned. If the rate of interest is higher, public are motivated to deposit more funds with the bank. There is also safety of funds deposited with the bank.

(b) Grant of loans and advances : The second important function of a commercial bank is to grant loans and advances. Such loans and advances are given to members of the public and to the business community at a higher rate of interest than allowed by banks on various deposit accounts. The rate of interest charged on loans and advances varies depending upon the purpose, period and the mode of repayment. The difference between the rate of interest allowed on deposits and the rate charged on the Loans is the main source of a bank's income.

(i) Loans: A loan is granted for a specific time period. Generally, commercial banks grant short-term loans. But term loans, that is, loan for more than a year, may also be granted. The borrower may withdraw the entire amount in lumpsum or in installments. However, interest is charged on the full amount of loan. Loans are generally granted against the security of certain assets. A loan may be repaid either in lumpsum or in instalments.

(ii) Advance: An advance is a credit facility provided by the bank to its customers. It differs from loan in the sense that loans may be granted for longer period, but advances are normally granted for a short period of time. Further the purpose of granting advances is to meet the day to day requirements of business. The rate of interest charged on advances varies from bank to bank. Interest is charged only on the amount withdrawn and not on the sanctioned amount.

Modes of short-term financial assistance: Banks grant short-term financial assistance by way of cash credit, overdraft and bill discounting.

(i) Cash Credit: Cash credit is an arrangement whereby the bank allows the borrower to draw amounts upto a specified limit. The amount is credited to the account of the customer. The customer can withdraw this amount as and when he requires. Interest is charged on the amount actually withdrawn. Cash Credit is granted as per agreed terms and conditions with the customers.

(ii) Overdraft: Overdraft is also a credit facility granted by bank. A customer who has a current account with the bank is allowed to withdraw more than the amount of credit balance in his account. It is a temporary arrangement. Overdraft facility with a specified limit is allowed either on the security of assets, or on personal security, or both.

(iii) Discounting of Bills : Banks provide short-term finance by discounting bills, that is, making payment of the amount before the due date of the bills after deducting a certain rate of discount. The party gets the funds without waiting for the date of maturity of the bills. In case any bill is dishonoured on the due date, the bank can recover the amount from the customer.

(2) Secondary functions: Besides the primary functions of accepting deposits and lending money, banks perform a number of other functions which are called secondary functions. These are as follows:

(a) Issuing letters of credit, travellers cheques, circular notes etc.

(b) Undertaking safe custody of valuables, important documents, and securities by providing safe deposit vaults or lockers;

(c) Providing customers with facilities of foreign exchange.

(d) Transferring money from one place to another; and from one branch to another branch of the bank.

(e) Standing guarantee on behalf of its customers, for making payments for purchase of goods, machinery, vehicles etc.

(f) Collecting and supplying business information;

(g) Issuing demand drafts and pay orders; and,

(h) Providing reports on the credit worthiness of customers.

Q3. Define the term 'customer'. What is the relationship between customer and banker? [June 2005, Q7] [Dec 2004, Q7]

Ans. A **customer**, also *client*, *buyer* or *purchaser* is the buyer or user of the paid products of an individual or organization, mostly called the supplier or seller. This is typically through purchasing or renting goods or services.

The word derives from "custom," meaning "habit"; a customer was someone who frequented a particular shop, who made it a habit to purchase goods of the sort the shop sold there rather than elsewhere, and with whom the shopkeeper had to maintain a relationship to keep his or her "custom," meaning expected purchases in the future. The word did not refer to those who purchased things at a fair or bazaar, or from a street vendor.

In commercial, market-driven or -oriented organizations, the customer is increasingly seen as the 'raison d'être' of the supplier. This view only gained general adherence in USA from the 1950s, among others through the work of Philip Kotler. In the Toyota Production System it has been pushed to the forefront of all deliberations, in connection with added value. In Europe the position of the customer has been recognized somewhat later, mainly due to the after effects of the Second World War and the necessary reconstruction.

Since the 1980s the term customer is also used by non-commercial organizations (local governments, hospitals), usually in a top-down effort to institute greater awareness of the goal of the organization: a shift from self-centered to serving. This shift, however, is often criticized, as the customer in a commercial organization has the freedom of choice, which is often absent when he deals with public services. With the rise of better defined ideas on customers came the customer unions, in general organizations with members that help them make choices in an increasingly growing and ever more complicated market.

Relationship between Banker and Customer: The relationship between a banker and a customer is as follows:

(a) Contractual Relationship: The primary relationship between a banker and a customer arises from a contract between the two, so it is a contractual relationship. The contract takes place the moment an account is opened by a customer with a bank and this contract remains valid till the customer operates his account as per the terms and conditions agreed between them.

(b) Debtor and Creditor Relationship: The relation of a banker and customer is primarily that of a debtor and creditor. When a customer opens an account with a bank and maintains a credit balance, the banker assumes the position of a debtor and the customer assumes the role of a creditor. Money deposited with the bank becomes a debt due from him to the customer. The banker can use the money deposited with him by the customers in any manner according to his discretion, his only obligation being to repay the debt as and when demanded by the customer.

(c) Bailee and Bailor Relationship: When a bank accepts deposits of money, he does not act as a bailee. This is so because a bailee accepts the bailment of goods on the condition that the things bailed will not be utilised by him and the identical goods will be returned. But a bank does not accept money from customer on the condition that it will not utilise the money and that the identical money (the same currency notes or coins deposited by customer) will be returned. A banker provides for safe deposit vaults and accepts documents and valuables for safe custody. Here the bank is acting as a bailee and the relationship is that of bailee and bailor.

(d) Trustee Beneficiary Relationship: Banks also act as trustees and executors of will of customers. A trustee is required to hold property and money and use the trust money in accordance with the trust deed and use it for the benefit of some other person known as beneficiary. A customer may deposit some money with the bank for a specific purpose with specific instructions to the bank regarding its use. In such cases, the banker is the trustee of the customer's money and the banker cannot employ them for any other purpose other than the purpose specified by the customer. We should note here that the money held under trust is different from the money received as deposits. The legal position of a banker as a trustee is different from that of a debtor to the customer. The relationship is determined by the particular circumstances in each case. For instance, when a bank receives a cheque from the customer for collection from another bank, the bank becomes a trustee till the amount of cheque is realised. Once the amount is credited to the customer's account, the banker assumes the position of a debtor.

(e) Principal-Agent Relationship: Banks perform many agency functions such as collection of cheques or drafts or bills, collection of interest and dividends on securities, arranging for remittances and payment of insurance premiums, etc., as per the instructions of the customers. In all such cases, the bank is acting as an agent of the customer. In these cases the position of a customer is that of the principal and the position of the banker is that of the agent. Here the bank has to act according to the instructions of the customer.

Q4. Explain the rights of Bank/Banker. [June 2003, Q4(b)]

Ans. For fulfilling the obligations towards the customers, bankers enjoy the following rights :

(1) Right of General Lien: One of the most important rights enjoyed by a bank is the right of general lien. Lien is a right of a person to retain goods belonging to another, until the demands of the person in possession are satisfied. Section 171 of the Indian Contract Act confers the right of general lien on the bankers. General lien entitles the banker in possession to retain goods and securities till all its claims against the customer are satisfied. We should note that the banker can exercise his right of general lien only as a banker and not as a bailee. Banker's lien is an implied pledge in the sense that if a default is made by the debtor, the banker can, after giving a reasonable notice to the customer, sell the goods in his possession and recover the amount. If some valuables are deposited with a bank for safe custody, then it is bailment and the bank cannot exercise the right of general lien.

We should note that the right of general lien cannot be exercised in the following cases :

(a) When valuables are deposited for safe custody,

(b) When money or documents are deposited for a specific purpose,

(c) When some securities are left with the bank by mistake,

(d) When the property is held by the customer as trustee and the bank has the notice of trust, and

(e) When there is an express agreement that the bank shall not exercise the right of general lien.

(2) The Right of Set-off: Right of set-off is the right of a debtor to adjust the amount due to him from a creditor against the amount payable by him to the creditor to determine the net balance payable by one to another. Like any other debtor, a bank also has a right of set-off. When a customer has two or more accounts in the same name and capacity in a bank, the bank has the right to adjust the amount standing to the credit of the customer against the debit balance in the other account. The bank has a right to combine the two accounts. For example, Mr. X has overdrawn his current account to the extent of Rs. 10,000 and he has a credit balance of Rs. 8,000 in his savings account. The bank can combine these two accounts and claim the balance of Rs. 2,000 after adjusting the credit balance of savings account against the debit balance of current account.

(3) Right of Appropriation: A customer may owe several distinct debts to the bank. When the customer deposits some money in the bank without specific instructions and the amount is not sufficient to discharge all debts, then the problem arises as towards which debt this amount should be adjusted. In the absence of any specific instructions, the bank has the right to appropriate the deposited amount to any loan, even to a time barred debt. But the banker must inform the customer about the appropriation.

(4) Right to Charge Interest and Commission: The bank has the implied right to charge interest on loans and advances and also to charge commission for services rendered by the bank. The bank can debit such charges to the customer's account.

(5) Right to Close the Account: If the bank is of the opinion that an account is not being operated properly, it may close the account by sending a written intimation to the customer.

Q5. Describe the types of Bank Account.

Ans. There are several different types of bank accounts. Understanding them all can be difficult, as each banking institution may offer a broad range of bank account types. However, most bank accounts fall into one of five categories. By learning the different account categories, you can make deciphering the choices offered at your banking institution much easier.

A **checking account** is a bank account that uses checks as the primary instrument for withdrawing money. With a checking account, you can make purchases, pay bills, and give or loan money to anyone you choose. You can also use a check to transfer money from your checking account to a bank account at a different financial institution. Usually, financial institutions allow account holders to make as many deposits and withdrawals as they wish. Many allow account holders to make withdrawals and deposits through automatic teller machines (ATM) as well. A **savings account** is another type of bank account that allows the holder to make deposits and withdrawals. However, savings accounts are not as flexible as checking accounts. Often, holders of this type of bank account are limited in the number of withdrawals and deposits they can make each month. Also, savings account holders are not able to access their money with checks. Many financial institutions allow savings account holders to make deposits and withdraw funds through ATM, however.

Another type of bank account is a **money market account**. This type of bank account pays interest at a higher rate than the rate paid on interest-bearing savings and checking accounts. Often, money market accounts impose a minimum balance for the account to start earning interest. The minimum required balance on a money market account is usually higher than that imposed on a checking or savings account. With a money market account, withdrawals are limited to six per month. No more than three of these withdrawals can be by check. Time deposits, frequently referred to as **certificates of deposit (CDs)**, are bank accounts that require the account holder to make a deposit and agree to leave funds in the account for a specific amount of time. In return for this agreement, the financial institution pays interest to the account.

Often, the interest paid on a CD is higher that the rate paid on other types of bank account. The account holder is required to keep his or her money in the account until the specified term is over. However, some financial institutions allow account holders to withdraw interest, without affecting the principal. In some cases, account holders may be allowed to withdraw their principal funds before their CD matures, but a penalty is typically charged.

Some financial institutions also offer basic, **no-frills bank accounts**. A no-frills bank account may allow the holder to pay bills and cash checks without paying the high fees associated with completing such transactions without an account. An account of this type will likely allow for only a limited number of checks, deposits, and withdrawals to be processed in any given month. In most cases, interest is not paid on a no-frills bank account.

Q6. Discuss various ways in which a commercial bank renders financial assistant to business.

Ans. The basic function of a commercial bank is to make loans and advances out of the money which is received from the public by way of deposits. The loans are particularly granted to businessmen and members of the public against personal security, gold and silver and other movable and immovable assets. Commercial bank generally lend money in the following form :

(i) Cash credit

(ii) Loans

(iii) Bank overdraft, and

(iv) Discounting of Bills

(i) Cash Credit: A cash credit is an arrangement whereby the bank agrees to lend money to the borrower upto a certain limit. The bank puts this amount of money to the credit of the borrower. The borrower draws the money as and when he needs. Interest is charged only on the amount actually drawn and not on the amount placed to the credit of borrower's account. Cash credit is generally granted on a bond of credit or certain other securities. This a very popular method of lending in our country.

(ii) Loans: A specified amount sanctioned by a bank to the customer is called a 'loan'. It is granted for a fixed period, say six months, or a year. The specified amount is put on the credit of the borrower's account. He can withdraw this amount in lump sum or can draw cheques against this sum for any amount. Interest is charged on the full amount even if the borrower does not utilise it. The rate of interest is lower on loans in comparison to cash credit. A loan is generally granted against the security of property or personal security. The loan may be repaid in lump sum or in instalments. Every bank has its own procedure of granting loans. Hence a bank is at liberty to grant loan depending on its own resources. The loan can be granted as:

(a) Demand Loan: Demand loan is repayable on demand. In other words it is repayable at short notice. The entire amount of demand loan is disbursed at one time and the borrower has to pay interest on it. The borrower can repay the loan either in lumpsum (one time) or as agreed with the bank. Loans are normally granted by the bank against tangible securities including securities like N.S.C., Kisan Vikas Patra, Life Insurance policies and U.T.I. certificates.

(b) Term Loans: Medium and long term loans are called 'Term loans'. Term loans are granted for more than one year and repayment of such loans is spread over a longer period. The repayment is generally made in suitable instalments of fixed amount. These loans are repayable over a period of 5 years and maximum upto 15 years. Term loan is required for the purpose of setting up of new business activity, renovation, modernisation, expansion/ extension of existing units, purchase of plant and machinery, vehicles, land for setting up a factory, construction of factory building or purchase of other immovable assets. These loans are generally secured against the mortgage of land, plant and machinery, building and other securities. The normal rate of interest charged for such loans is generally quite high.

(iii) Bank Overdraft: Overdraft facility is more or less similar to cash credit facility. Overdraft facility is the result of an agreement with the bank by which a current account holder is allowed to withdraw a specified amount over and above the credit balance in his/her account. It is a short term facility. This facility is made available to current account holders who operate their account through cheques. The customer is permitted to withdraw the amount as and when he/she needs it and to repay it through deposits in his account as and when it is convenient to him/her.

Overdraft facility is generally granted by bank on the basis of a written request by the customer. Some times, banks also insist on either a promissory note from the borrower or personal security to ensure safety of funds. Interest is charged on actual amount withdrawn by the customer. The interest rate on overdraft is higher than that of the rate on loan.

(iv) Discounting of Bills: Apart from granting cash credit, loans and overdraft, banks also grant financial assistance to customers by discounting bills of exchange. Banks purchase the bills at face value minus interest at current rate of interest for the period of the bill. This is known as 'discounting of bills'.

Bills of exchange are negotiable instruments and enable the debtors to discharge their obligations towards their creditors. Such bills of exchange arise out of commercial transactions both in internal trade and external trade. By discounting these bills before they are due for a nominal amount, the banks help the business community. Of course, the banks recover the full amount of these bills from the persons liable to make payment.

Q7. Discuss various instruments used for payment through bank.

Ans. Following are the various instruments used for payments through banks :

Cheques: According to Section 6 of Negotiable Instruments Act, 1881, "A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand'. From this definition it is clear that a cheque is an instrument in writing, containing an unconditional order to a bank to pay a certain sum of money on demand to a specific person or according to his order or it may be made payable to the bearer of the instrument. There are three parties to a cheque – drawer, drawee and the payee. A drawer is the person who has an account in the bank and who is writing the cheque. A drawee is one on whom the cheque is drawn, he is liable to make the payment. In case of a cheque paying bank is the drawee. A payee is the person to whom the account of cheque is to be paid. If the cheque is made payable to "self", the drawer himself becomes the payee. A cheque may either be a bearer cheque or an order cheque. A bearer cheque is one where the payment can be had by the person who is presenting the cheque to the bank for payment. A bearer cheque can be transferred from one person to another by mere delivery only i.e., just like cash payments. On the other hand an order cheque is one which is payable to a certain person or his order. In an order cheque, the payee must be named. An order cheque cannot be transferred from one person to another by mere delivery. It requires the endorsement of the payee.

A cheque is not meant for indefinite circulation. It must be presented for payment within six months of the date appearing on the cheque. If a cheque remains in circulation for a period exceeding six months from the date of issue, it is termed as a "stale cheque" and the bank must dishonour such cheques. If a cheque bears a date which is yet to come is termed as a 'post-date cheque'. A post dated cheque does not become invalid. It is valid and negotiable. But it is not payable until the arrival of the date written on it. The banks do not make the payment of a post date cheque because the written order is to be honoured on or after the date mentioned on the cheque.

In order to ensure the payment by cheque absolutely safe, the cheques are crossed. Crossing of a cheque means drawing across the face of the cheque two parallel lines with or without the words "And Company" between the lines. Crossing can be hand written or stamped. When a cheque is crossed, its payment cannot be received at the counter but it is always deposited in the account of the payee. The paying banker should make the payment of a cheque according to the instructions mentioned on the cheque. The paying banker should not deviate from those instructions. If the bank pays a stale cheque or pays a post dated cheque before the due date, the bank shall not receive the statutory protection. The paying banker should always make the payment in good faith and without negligence.

Drafts: Commercial banks are very useful for remittance of funds from one place to another through the network of their branches spread over the entire country. For remitting money from one place to another, banks issue demands drafts on their branches at the place where payment is to be made. It is issued on the request of a customer who has to make a guaranteed payment.

Section 85A of the Negotiable Instruments Act defines a bank draft as “an order to pay money drawn by one office of a bank upon another office of the same bank for a sum of money payable to order on demand”. A bank draft is, thus, a payment instruction similar to a cheque and is always drawn by one branch on another to pay a specified sum of money to the person named therein or his order. We must note that a draft is always payable on demand and it cannot be made payable to bearer. It can be crossed like a cheque.

A bank issues a draft for consideration received in advance. The person who intends to remit money has to make an application on the bank’s prescribed form showing the necessary particulars such as the name of the payee, name of the place on which draft is required, amount in words and figure, signature and full name of the applicant with address. The issuing bank charges a commission for rendering this service and the amount of commission depends upon the amount to be remitted. The purchaser then sends the draft to the payee by whom the draft is presented to the drawee branch for payment.

We must have noticed that there are three parties to a bank draft: (a) the issuing branch or drawer, (b) paying branch or drawee, and (c) the payee. It means that the purchaser of the draft is not a party to the instrument. It is to be noted that this service is extended by banks to public in general and the purchaser of the draft need not necessarily be a “customer” i.e., an account holder of the bank.

Stopping payment of Bank Draft: A bank draft is the issuing bank’s commitment in favour of the payee to pay a certain sum of money. Though the bank gives the undertaking at the instance of the purchaser of the draft, who gives due consideration for the same, but a bank draft is equivalent to the bank’s promissory note and is accepted because of the credit and faith in the bank which is issuing the draft. The bank should not, therefore, comply with ‘stop payment’ instructions of the purchaser of the draft as readily as that of the drawer of a cheque. If the bank draft is passed on to the payee, he acquires a right in the instrument which cannot be set aside by ‘stop payment’ instructions of the purchaser. Thus, it is clear that the purchaser of the draft can ask the bank from which he has purchased it to cancel the draft and pay back the money to him at any time before the draft has been delivered to the payee.

Standing Instructions: Sometimes a customer gives instructions to his bank to make some payments on his behalf regularly and such instructions are to be carried out till a notice to the contrary is given by the customer. Such instructions are called standing instructions. Some of the standing instructions are – payment of insurance premium to LIC, membership subscription to clubs, transfer of funds from one account to another, collection of pension on behalf of account holder, collection of interest on Government Securities held in safe custody, collection of dividends on behalf of the customer, etc.

Such instructions which are obtained from the customer in writing, must be clearly and unambiguously worded. The bank is free not to accept standing instructions which are difficult to comply with, but once they are accepted, it is the duty of the bank to carry out the instructions carefully and promptly. Once the standing order mandate has been accepted, no further action is required by the customer except that he must keep sufficient funds in his account. It is the bank's duty to pay only on the due date. If funds were insufficient to make a payment on the due date, there is no obligation to the customer in respect of that month's payment.

Q8. Discuss various modes of creating charges. [June 2007, Q6]

Ans. A cardinal principle of sound banking is to ensure safety of funds sent by a banker to his customers. The viability of the project and the honesty and capability of the borrower ensure to a larger extent the safety of funds to the bank. To ensure more safety, much reliance is placed on tangible assets owned by the borrower or created out of the bank funds by him. The mode of creating interest or right over such tangible assets is called charges.

Meaning of Charge : Charging a security means making it available as a cover for an advance. A charge may not amount to a transfer of ownership but create only some interest or right in the security available as a cover for an advance.

Two special features of charging are :

(a) the security should have good qualities

(b) The security is easily realisable.

The common feature in any type of charge is that ownership does not change i.e. the banker does not become the absolute or exclusive owner of the property. He has only defined rights in it, until the debt due is repaid.

Various Types of Charges : There are about six different modes of charges, i.e. pledge/ Hypothecation /mortgage/ lien/ set off and assignment. Some of them are discuss below:

Pledge : Pledge is a bailment or delivery of goods or documents of title to goods by the borrower to the lender with the intention of creating a charge thereon as security for the payment of a debt or performance of a promise. The person creating the charge is the pledger and the person to whom the goods are delivered with the intentions to form a security is called the pledge.

The ownership of the goods remains with the pledger. While the pledge rights are with the creditor. The delivery of the pledged goods may be physical or constructive. The advantages are (a) disposal of goods is easy (b) pledge supersedes the first equitable charge.

Parties who can create valid pledge

- **(a)** an owner of the goods
- **(b)** a person in possession of the goods with consent of the owner
- **(c)** a mercantile agent with the consent of the owner in the ordinary course of business provided the pledgee acts in good faith and has no notice at the time of pledge that pledger had no authority to pledge.
- **(d)** The seller of the goods who has parted with the goods sold with the consent of the buyer
- **(e)** Third party in possession of the goods with the consent of the seller
- **(f)** A person who is in possession of the goods under voidable contract and goods are pledged before it is voided
- **(g)** When pledgee re-pledges
- **(h)** One of the joint owners of the goods when pledges
- **(i)** Buyer of the goods before making payment and holding the goods through sale provided pledgee acts in good faith and has no notice of previous sale.

Pledger's responsibilities:

- **(a)** He is under obligation to disclose to the pledge any faults in the goods pledged of which he is aware of and which could expose the pledge to extraordinary risks and if he does not do so he is responsible to the pledgee for the damages.
- **(b)** He is responsible to repay to the pledge all necessary expenses which may be incurred by the pledgee for preservation of goodwill
- **(c)** He is responsible for any loss that the pledgee may sustain on account of pledger 's defective title to the goods pledged.

Pledger's right:

- **(a)** He is entitled to get back the goods after payment of the debt
- **(b)** He is entitled to receive surplus (if any) or liable to pay shortfall (if any) in case if the pledgee sells the pledged goods
- **(c)** He can recover/ get back the goods at any time before actual sale of the pledged goods is effected

Pledgee's responsibilities:

- **(a)** He should take reasonable care of the pledged goods
- **(b)** The pledgee should not part with the pledged goods before the debit is recovered except in case of trust receipt)

Pledgee's right:

- **(a)** He can recover / claim all lawful dues including any lawful incidental expenses

(b) Right to sale after giving due notice i.e. he can either sell the goods or alternatively can sue the borrower before the actual sale is affected

(c) After sale he is entitled to recover / claim the shortfall / if any.

Hypothecation : There is no legal definition for hypothecation. Hypothecation is an equitable charge against goods for payment of debt. The possession and the ownership remain with the borrower. If the proper clause is incorporated in letter of hypothecation of goods, then as and when required and if possible this hypothecation can be converted into pledge by taking possession of the goods by the creditor from the borrower. Since the possession remains with the borrowers he can subsequently create another charge (say pledge) and in such a case the subsequent pledge will supercede. The earlier charge of hypothecation except in case of limited company. Hence a board displaying the charge of hypothecation in favour oft the bank should always be displayed in borrower's premises, provided the subsequent pledgee/ hypothecatee has no notice of bank's charge in case of joint stock companies the charges of hypothecation must be registered with the registrar of companies within thirty days from the date of creation of charges, the stock statement should be submitted by the borrower at regular intervals. The bank should verify the stock and account books, invoices / vouchers etc. it is equally important to keep close and sharp watch on the financial position of the borrower.

Mortgage : It is defined in Transfer of Property Act as:

(a) the transfer of interest in

(b) a specific immovable property

(c) for the purpose of securing the payment of money

(d) advanced or to be advanced by way of loan, an existing or future debt or performance of an engagement which may give rise to a pecuniary liability. The owner of the property who borrows and transfers his right is called mortgagor and the transferee is called the mortgagee.

Special features are:

(a) it is not a sale but only a transfer of interest

(b) in the specific immovable property immovable means

(i) rooted in the earth like trees and shrubs or

(ii) imbedded in the earth as in the case of walls or buildings or

(iii) attached to what is so embedded for the permanent enjoyment of that top which it is attached. Therefore even sometimes plant and machinery are treated as immovable, if they satisfy the condition as referred to above.

Kinds of Mortgage : The under noted are the mortgages which are recognised by the transfer of property act:

(a) Simple mortgage
(b) Mortgage by conditional sale
(c) Usufractuary mortgage
(d) English mortgage
(e) Equitable mortgage
(f) Anomalous mortgage

Q9. What is Business Risk? Discuss about the types of business risk. [Dec 2003, Q1(d)]

Ans. A business risk is a circumstance or factor that may have a negative impact on the operation or profitability of a given company. Sometimes referred to as company risk, a business risk can be the result of internal conditions, as well as some external factors that may be evident in the wider business community. When it comes to outside factors that can create an element of business risk, one of the most predominant risks is that of a change in demand for the goods and services produced by the company. If the change is a positive one, and the demand for the offerings of the company increase, the amount of risk is decreased a great deal. However, if consumer demand for the offerings decreases, either due to loss of business to competitors or a change in general economic conditions, the amount of risk involved to investors will increase significantly. When a company's risk factor is considered to be increased due to outside factors that are beyond the control of the company to correct, chances of attracting new investors is severely limited.

Internal factors may also result in the development of significant business risk for the investor. Often, these are factors that can be identified and corrected. If flagging sales can be attributed to an ineffectual marketing effort or a sales force that is not performing up to expectations, making changes in the marketing approach or restructuring the sales effort will often result in minimizing the perception of business risk on the part of potential investors. The same is true if a company's manufacturing facilities are not operating at optimum efficiency. Revamping the operational structure of the plants and facilities will decrease the element of business risk and result in higher profits at the same level of production and sales, which will in turn make the company more attractive to potential investors. In general, any investor will consider the relationship of a company's securities and the business risk associated with the company before choosing to invest in the future of the corporation. While there is an element of business risk associated with any corporate operation, proper management will result in creating a balance between assets and securities that will keep the degree of business risk attractive to individuals and entities that consider investing funds into the operation.

Types of Business Risks :

Pure vs. Speculative Risks : The occurrence of perils like fire, windstorm, explosion, flood, earthquake, riot, etc., generally cause losses only. Their occurrence never result into gains. The uncertainty concerning their occurrence may be termed as pure risks. Thus, Pure risks are those risks in which the occurrence of events causes losses only. For instance, car drivers always face the risk of accidents. If an accident occurs, the driver may suffer physical and financial losses. If the accident did not occur, there would not be any gain. Thus, in the case of a pure risk, there is loss when it occurs, otherwise there is no loss or gain. On the other hand speculative risks involve events which may produce either gains or losses. For instance, expansion of operations in a new market (area) may lead to higher profits or loss of invested funds. Most business decisions relating marketing, production, finance, etc., are taken with the idea of making gains, but there are possibilities of incurring losses also. Thus, all business enterprises face both pure risks as well as speculative risks. Many pure risks can be handled through insurance, while most of the speculative risks are not generally handled through insurance. So business enterprises must find their own ways of handling speculative risks.

Dynamic vs. Static Risks: Risks can also be classified as dynamic risk and static risks. Dynamic risks are related to uncertainties caused by an ever-changing business environmental factors such as consumer wants, technology, competition, governmental policies, firms internal organization, etc. On the other hand static risks are those which occur even if there are no changes in the business environment. Normally static risks are closely related to pure risks such as fire, flood, windstorm, etc., where as dynamic risks are more closely associated with speculative risks. Therefore, as discussed in the case of pure and speculative risks, most of the static risks can be handled through insurance while most of the dynamic risks may not be handled by insurance. However, it is increasingly becoming difficult to separate or distinguish clearly between the losses caused by dynamic risks and static risks. For instance, fire which is a static risk may be caused by an irate crowd during a demonstration which is a dynamic risk.

Risk Classified by Loss Severity: Risks may also be classified as follows into three groups on the basis of the extent of loss and its importance on the financial position of the business firm:

Class 1: Those losses which do not disturb a firms basic finances.

Class 2: Those losses which would require borrowing or selling firms property.

Class 3: Those losses which might bankrupt the firm.

Here Class 1 risks cause small losses, Class 2 risks cause much bigger losses and the firm may not survive with the occurrence of Class 3 risks. Therefore, Class 1 and 2 risks can be handled by various internal methods but

Class 3 risks are beyond internal capabilities of the business firms.

Objective vs. Subjective Risks: Objective risk is the measure of the degree of variation in the proportion of actual from the expected events. This proportion declines as the number of observed events increase. Hence we can say that the objective risk as a proportion declines when larger and larger number of events are involved. Subjective risk may be defined as the uncertainty of an event as seen or perceived by an individual. This perception depends on the attitudes of the concern individuals towards risk. Among people, there are 'risk lovers' who prefer a situation with a great deal of uncertainty and also 'risk haters' or 'risk averters' who do not like to face risks.

Q10 Write a short note on risk management. [Dec 2006, Q6]

Ans. Risk management involves five basic steps :

(1) Risk identification is the first step and also the most difficult function. Failure to identify all the loss exposers of the firm means we will not be in a position to deal with those risks. Therefore, as a first step we should identify all types of loss exposers of our business.

(2) After identifying the risks, we should **assess the intensity of financial loss** associated with each of those risks. At this stage we have to determine two aspects: (a) probability of the occurrence of each of the perils or risk identified in the first stage, and (b) extent of financial loss to the firm, if that peril occur. With this assessment, we can identify the relatively more serious risks and can pay more attention to them.

(3) After risk identification and proper measurement, at the third stage we should **consider various tools of risk management** and decide upon the best combination of the tools to be used for attacking the problem. There are basically six tools of risk management viz., (a) assumption (or retention), (b) loss prevention, (c) avoidance, (d) transfer (insurance), (e) separation, and (f) combination. Business firms may adopt any one of these six methods or a combination of them. Let us discuss these methods briefly.

(a) Risk Assumption or Retention: This is a common way of handling risks. Business enterprises assume or retain risks consciously (intentionally) or unconsciously (unintentionally). Under conscious assumption, one is aware of the risk to which his/her business is exposed, but essentially does nothing to avoid it. A manager of a business who consciously assumes risk is doing something about it by the very act of being aware of those perils and hazards which may cause loss. Being aware of risk, he may knowingly or unknowingly make adjustments in operations which will help to alleviate the impact of that risk. Awareness of risk itself is a significant achievement in better management. In the case of unconscious risk assumption, risk is not recognized. As we are not even aware of the existence of some risk, losses stemming from it can cause disastrous surprises to our business.

(b) Loss Prevention: Another method of handling risk is to take appropriate measures to prevent the occurrence of a peril or minimize its financial impact on business. This approach is known as loss prevention. For instance, by using fire resistant building material, we are prevent the occurrence of fire in the building. However, in most cases loss prevention measures may not totally eliminate the risk, but can reduce its probability in terms of frequency as well as severity.

(c) Avoidance: Avoiding situations which have the potential to cause loss, is another approach. For instance, a firm can avoid the risk of loss due to bad debts by simply stopping credit sales. Similarly, a firm may avoid operations in certain areas which are known for some perils like terrorism.

(d) Transfer: Transferring the risk to another party is a very widely followed approach to handle risks. Insurance is the most common method of transferring pure risks such as fire, windstorm, flood, riot, theft, etc. Business enterprises normally transfer the pure risks to the insurance company and devote their full efforts to their normal business.

(e) Separation: Fifth method of risk control is separation of the firm's exposers to loss instead of concentrating them at one location where all of them might be involved in the same loss. For example, when a firm keeps its entire raw material in one warehouse, the entire raw material may be damaged if fire occur in that warehouse. Therefore, the firm may decide to store the raw material in ten separate warehouses. If fire occur in one warehouse, materials stored in that warehouse are damaged and the remaining nine warehouses are safe. Here through separation the firm increases the number of independent exposure units under its control. This methods is also a kind of loss prevention.

(f) Combination: Strategies like diversification of products, law of large numbers, formulation of more companies with unrelated lines of business, etc., come under this method. For example, if a firm is engaged in more products, the losses incurred in one product may be upset by the gains in another product. Similarly, if there are more companies, the losses incurred by one company may be upset by the gains by the other companies. Insurance companies work on this combination principle where a sufficiently large number of similar objects are combined to make the loss predictable within narrow limits.

Subjective risks can be reduced by having more knowledge about such perils. A person with better knowledge of the perils can handle them more easily than a person who do not have the knowledge. Therefore, subjective risks may be reduced through knowledge and research. An important aspect we should remember here is that while managing risks we should not just rely on any one method, instead we should usually employ some combination of various methods.

(4) After taking a decision regarding the combination of risk management tools, the next step is the **implementation of the decision** made. For instance, if we have decided in the previous stage to transfer the risk, we have to get the insurance policy at this stage.

(5) Finally, we have to evaluate the effectiveness of the risk management tools we have implemented.

The result of the decision made in the four stages must be evaluated to determine their effectiveness and change the strategy, if required.

Q11. What is insurance? Distinguish between insurable and non-insurable risks. [June 2008, Q6] [Dec 2007, Q1(d)]

Ans. Insurance, in law and economics, is a form of risk management primarily used to hedge against the risk of a contingent loss. Insurance is defined as the equitable transfer of the risk of a loss, from one entity to another, in exchange for a premium, and can be thought of as a guaranteed small loss to prevent a large, possibly devastating loss. An insurer is a company selling the insurance; an insured is the person or entity buying the insurance. The insurance rate is a factor used to determine the amount to be charged for a certain amount of insurance coverage, called the premium. Risk management, the practice of appraising and controlling risk, has evolved as a discrete field of study and practice.

Insurable Risks and Non-Insurable Risks: The characteristics of the insurable risks are as follows :

(a) The risk should be accidental or random in nature. The loss causing factor should not be within the control of the insured. Thus, the loss which has occurred already or which is very likely to occur can not be insured. For instance, a building which is on fire or which is already destroyed by fire can not be insured against fire. Similarly, a person who is infected with AIDS disease can not be insured because he is sure to die as there is no treatment to AIDS so far.

(b) The amount of loss should be measurable and possible to estimate. This condition is necessary to set the premium at appropriate levels.

(c) There should be a sufficiently large number of units exposed to the same risk. In other words, there must be a large number of people interested to insure against the same risk. This requirement follows from the law of large numbers, since an insurance operation is safe only when the insurer is able to predict fairly accurately its expected losses.

(d) The units facing the same risk must be spread over large geographical area. In other words, the risk must be spread over a wide geographical area so that the happening of a single event in a small region may not cause heavy burden to the insurer. For instance, if an insurance company had accepted against fire for the buildings located in one area only, an incidence of fire in that area can destroy all those builds. The insurance company may become bankrupt with that single incidence as it has to pay to all the insured. Therefore, it is necessary that the values exposed to loss should not be concentrated in one area.

Normally, pure risks fulfill all the above four features and they are insurable. There are certain risks which do not fulfill these four requirements explained above and cannot be insured against. They are called non-insurable risks. These non-insurable risks include :

(a) Risks due to war (except cargo at sea) and certain risks such as radio activity arising from nuclear fusion.

(b) Risks incapable of measurement such as unforeseen changes in fashion, marketing of new products, etc.

(c) Risks too small and recurring too frequently or risks so large and recurring so infrequently. For instance, a hotel can not insure the crockery against breakages.

Q12. Write a short note on followings:
(1) Life Insurance (2) Marine Insurance [June 2003, Q4(c)]
(3) Fire Insurance (4) Motor Insurance
(5) Miscellaneous Insurance

Ans. (1) Life Insurance: Life insurance provides a monetary benefit to a decedent's family or other designated beneficiary, and may specifically provide for income to an insured person's family, burial, funeral and other final expenses. Life insurance policies often allow the option of having the proceeds paid to the beneficiary either in a lump sum cash payment or an annuity. Annuities provide a stream of payments and are generally classified as insurance because they are issued by insurance companies and regulated as insurance and require the same kinds of actuarial and investment management expertise that life insurance requires. Annuities and pensions that pay a benefit for life are sometimes regarded as insurance against the possibility that a retiree will outlive his or her financial resources. In that sense, they are the complement of life insurance and, from an underwriting perspective, are the mirror image of life insurance. Certain life insurance contracts accumulate cash values, which may be taken by the insured if the policy is surrendered or which may be borrowed against. Some policies, such as annuities and endowment policies, are financial instruments to accumulate or liquidate wealth when it is needed.

In many countries, such as the U.S. and the UK, the tax law provides that the interest on this cash value is not taxable under certain circumstances. This leads to widespread use of life insurance as a tax-efficient method of saving as well as protection in the event of early death.

In U.S., the tax on interest income on life insurance policies and annuities is generally deferred. However, in some cases the benefit derived from tax deferral may be offset by a low return. This depends upon the insuring company, the type of policy and other variables (mortality, market return, etc.). Moreover, other income tax saving vehicles (e.g., IRAs, 401(k) plans, Roth IRAs) may be better alternatives for value accumulation. A combination of low-cost term life insurance and a higher-return tax-efficient retirement account may achieve better investment return.

(2) Marine Insurance: Marine Insurance covers the loss or damage of ships, cargo, terminals, and any transport or property by which cargo is transferred, acquired, or held between the points of origin and final destination.

Cargo insurance – discussed here – is a sub-branch of marine insurance, though Marine also includes Onshore and Offshore exposed property (container terminals, ports, oil platforms, pipelines); Hull; Marine Casualty; and Marine Liability. A marine policy typically covered only three-quarter of the insured's liabilities towards third parties. The typical liabilities arise in respect of collision with another ship, known as 'running down' (collision with a fixed object is an 'allision'), and wreck removal (a wreck may serve to block a harbour, for example).

In the 19th century, shipowners banded together in mutual underwriting clubs known as Protection and Indemnity Clubs (P&I), to insure the remaining one-quarter liability amongst themselves. These Clubs are still in existence today and have become the model for other specialised and uncommercial marine and non-marine mutuals, for example in relation to oil pollution and nuclear risks. Clubs work on the basis of agreeing to accept a shipowner as a member and levying an initial 'call' (premium). With the fund accumulated, reinsurance will be purchased; however, if the loss experience is unfavourable one or more 'supplementary calls' may be made. Clubs also typically try to build up reserves, but this puts them at odds with their mutual status. Because liability regimes vary throughout the world, insurers are usually careful to limit or exclude American Jones Act liability.

(3) Fire Insurance: Fire insurance provides protection against damage to property caused by accidents due to fire, lightening or explosion, whereby the explosion is caused by boilers not being used for industrial purposes. Fire insurance also includes damage caused due to other perils like storm, tempest or flood; burst pipes; earthquake; aircraft; riot, civil commotion; malicious damage; explosion; impact. There are three types of insurance coverage. Replacement cost pays the cost of replacing your property regardless of depreciation or appreciation. Extended replacement cost will pay over the coverage limit if the costs for construction have increased. This generally will not exceed 20% of the limit. Actual Cash Value provides replacement minus depreciation. When you obtain an insurance policy, the coverage limit established is the maximum amount the insurance company will pay out in case of loss of property. This amount will need to fluctuate if homes in your neighborhood are rising; the amount needs to be in step with the actual value of your home. In case of a fire, household content replacement is tabulated as a percentage of the value of the home. In case of high value items, the insurance company may ask to specifically cover these items separate from the other household contents. One last coverage option is to have alternative living arrangements included in a policy. If a fire leaves your home uninhabitable, the policy can help pay for a hotel or other living arrangements.

Fire insurance business in India governed by the All India Fire Tariff that lays down the terms of coverage, the premium rates and the conditions of the Fire Policy. The fire insurance policy renamed as Standard Fire and Special Perils Policy. The risks covered are as follows :

Dwellings, Offices, Shops, Hospitals (Located outside the compounds of industrial/manufacturing risks) Industrial / Manufacturing Risks Utilities located outside industrial/manufacturing risks Machinery and Accessories Storage Risks outside the compound of industrial risks Tank farms / Gas holders located outside the compound of industrial risks

Perils Covered: Cause of Loss:

Fire Lightning Explosion/Implosion Aircraft damage Riot, Strike Terrorism Storm, Flood, inundation Impact damage Subsidence, landslide Bursting or overflowing of tanks Bush fire etc.

Claims: In the event of a fire loss covered under the fire insurance policy, the Insured shall immediately give notice there of to the insurance company. Within 15 days of the occurrence of such loss the Insured should submit a claim in writing giving the details of damages and their estimated values. Details of other insurances on the same property should also be declared.

(4) Motor Insurance: This includes automobile, truck, motorcycle, aircraft, boat, or any other form of motorized transportation. It is perhaps the most common type of insurance, and is required by law in many countries. Motor insurance covers the insured party against financial loss that he may incur to repair his vehicle or a third party's in the event of an accident. In return for annual or semi-annual premiums, the insurance company is bound to pay any losses as described in the policy. Such a policy may include property, liability or third party, and medical coverage. Property coverage insures damage to or theft of a vehicle; liability covers bodily injury or property damage that may occur as a result of the insured's actions, and medical coverage pays any fees necessary for bodily injuries, rehabilitation and in some cases foregone wages and funeral costs.

In many countries, all of these types of automobile insurance are required of vehicle owners. In some countries, or states, only third party is required. However, in the case of new vehicles, any banks which may be financing the vehicle may require full insurance as a condition of financing.

(5) Miscellaneous Insurance: There are several other types covering various other aspects of risks. Some of them are discussed below.

Engineering Insurance: This is a highly technical branch of insurance. It is a branch of insurance that has expanded rapidly under recent legislation and especially under the Factories Acts, which prescribe compulsory inspection at regular intervals of certain types of industrial equipment, such as boilers, electrical plant, cranes and other lifting gear. Policies over the inspection service, the cost of repairing or replaying plant and also injury to persons and damage to property. Cover is also available for machinery in transit or in course of erection.

Aviation Insurance: Under aviation insurance, cover is available for loss of or damage to aircraft, personal accidents to passengers, third party risks in respect of both person and property and for cargo sent by air. However, accidents to staff who fly regularly are covered by group instance schemes.

Householder's Policies: Most fire companies now offer an extensive range of cover on the buildings and contents of private dwellings under householders' or all-in policies. Normally, these policies are designed to provide protection in one document against a variety of risks (additional to those already covered by a standard fire policy) including burglary, housebreaking, theft, accidents to domestic servants, liability to third parties, glass breakages and other hazards. Under these policies it is normally insisted to insure buildings and contents for their full value to enable the insurer to earn an adequate premium.

Fidelity Guarantee Insurance: As we know, cashiers and others who handle money are frequently required by their employers to provide security as protection against their personal dishonesty. In such cases, fidelity guarantee insurance policy may be taken by the employer. The policy indemnifies the employer against losses from the dishonesty of his employees. The employer himself often takes out the policy. He may insure a number of employees either individually or on a group basis under a variety of policies.

Burglary, Theft and Robbery: Burglary is the act of unauthorized entry with criminal intentions, into any building or residence. Theft is the act of dishonestly taking property belonging to another with the intention of depriving him of it. Robbery is theft with violence or the threat of violence. Burglary insurance covers the loss caused on account of burglary, house breaking or theft.

Q13. What is an insurance contract? Discuss the parts of insurance contract. [June 2006, Q1(f)] [Dec 2004, Q1(d)]

Ans. An **insurance contract** determines the legal framework under which the features of an insurance policy are enforced. Insurance contracts are designed to meet very specific needs and thus have many features not found in many other types of contracts. Many features are similar across a wide variety of different types of insurance policies.

General features: The insurance contract is a contract whereby the insurer will pay the insured (the person whom benefits would be paid to, or on the behalf of), if certain defined events occur. Subject to the "fortuity principle", the event must be uncertain. The uncertainty can be either as to when the event will happen (i.e. in a life insurance policy, the time of the insured's death is uncertain) or as to if it will happen at all (i.e. a fire insurance policy).

(a) Insurance contracts are generally considered contracts of adhesion because the insurer draws up the contract and the insured has little or no ability to make material changes to it. This is interpreted to mean that the insurer bears the burden if there is any ambiguity in any terms of the contract.

(b) Insurance contracts are **aleatory** in that the amounts exchanged by the insured and insurer are unequal and depend upon uncertain future events.

(c) Insurance contracts are **unilateral**, meaning that only the insurer makes legally enforceable promises in the contract. The insured is not required to pay the premiums, but the insurer is required to pay the benefits under the contract if the insured has paid the premiums and met certain other basic provisions.

(d) Insurance contracts are governed by the principle of **utmost good faith** (uberrima fides) which requires both parties of the insurance contact to deal in good faith and in particular it imparts on the insured a duty to disclose all material facts which relate to the risk to be covered. This contrasts with the legal doctrine that covers most other types of contracts, caveat emptor (let the buyer beware).

Parts of an insurance contract:

(a) **Definitions -** define important terms used in the policy language.

(b) **Insuring agreement -** describes the covered perils, or risks assumed, or nature of coverage, or makes some reference to the contractual agreement between insurer and insured. It summarizes the major promises of the insurance company, as well as stating what is covered.

(c) **Declarations -** identifies who is an insured, the insured's address, the insuring company, what risks or property are covered, the policy limits (amount of insurance), any applicable deductibles, the policy period and premium amount.

(d) **Exclusions -** take coverage away from the Insuring Agreement by describing property, perils, hazards or losses arising from specific causes which are not covered by the policy.

(e) **Conditions -** provisions, rules of conduct, duties and obligations required for coverage. If policy conditions are not met, the insurer can deny the claim.

Q14. Discuss the importance of transports. What are the characteristics of a good transport?

Ans. Transport or **transportation** is the movement of people and goods from one location to another. Transport is performed by various modes, such as air, rail, road, water, cable, pipeline and space. The field can be divided into infrastructure, vehicles, and operations. Infrastructure consists of the fixed installations necessary for transport, and may be roads, railways, airways, waterways, canals and pipelines, and terminals such as airports, railway stations, bus stations and seaports. Vehicles traveling on the network include automobiles, bicycles, buses, trains, people and aircraft. Operations deal with the way the vehicles are operated, and the procedures set for this purpose including the financing, legalities and policies. In the transport industry, operations, and ownership of infrastructure, are both public and private, depending on the country and mode.

Transport, simply stated, means carrying of goods and passengers from one place to another. In the context of trade, transport involves carriage of goods from places of production to centres of distribution and sale, which may be within the country or abroad. Thus, transport facilitates trading activities to create place utility to goods by removing the barrier of distance between production and consumption. In modern societies the scope of trade has increased not only due to the range of goods produced, but also on account of large scale production and widening of the market geographically. Transport plays an important role in the continuous supply of raw material to the industry and distribution of goods to ultimate consumers. It also contributed to the growth of large-scale industries by facilitating the inflow of raw materials and outflow of finished goods. Transport enables traders to adjust the supply of goods at different places according to changing demand from time to time. Thereby price fluctuations are reduced to the minimum.

Consumers derive benefits from transportation in three ways. **Firstly**, a large variety of products manufactured at different places are available to consumers all over the country as well as abroad. This is known as the benefit of diversified consumption. **Secondly**, as economics of scale achieved due to large-scale production and extension of markets with the help of transportation, goods are available at lower prices to the consumers. **Thirdly**, goods are available at stable prices as transport enables supplies to be moved quickly from surplus to deficit areas.

Economic benefits which are derived from transport facilities may be outlined as follows: (i) Development of industry and trade depends a great deal on the availability of transport. Easy transportability of raw materials, finished products and also movement of labour, have contributed immensely to the growth of trade and industrial activities. (ii) Extension of markets through transport development enables buyers to have a wider choice of goods at competitive prices. Extended markets also provide opportunities to the sellers to sell at the most profitable markets. Thus, buyers as well as sellers are benefited due to proper transport facilities. (iii) International competition is encouraged with the improvements in transport system. It makes markets accessible to sellers and buyers of different countries and leads to wider choice of quality products. (iv) Well-developed sea and ocean transport have led to increased imports and exports. This has made it possible for each country to specialize in the production of goods for which it has competitive advantage. (v) Transport has facilitated economic interdependence of countries, which has, in turn, enabled people to interact and promote material welfare of the human kind.

Q15. Write a short note on followings:
(1) Road transport **(2) Rail transport**
(3) Air transport **(4) Sea transport**
(5) Miscellaneous transport

Ans. (1) Road Transport: Road transport (British English) or road transportation (American English) is transport on roads of passengers or goods.

The first forms of road transport were horses, oxen or even humans carrying goods over dirt tracks that often followed game trails. As commerce increased, the tracks were often flattened or widened to accommodate the activities. Later, the travois, a frame used to drag loads, was developed. The wheel came still later, probably preceded by the use of logs as rollers.

With the advent of the Roman Empire, there was a need for armies to be able to travel quickly from one area to another, and the roads that existed were often muddy, which greatly delayed the movement of large masses of troops. To resolve this issue, the Romans built great roads. The Roman roads used deep roadbeds of crushed stone as an underlying layer to ensure that they kept dry, as the water would flow out from the crushed stone, instead of becoming mud in clay soils. During the Industrial Revolution, and because of the increased commerce that came with it, improved roadways became imperative. The problem was rain combined with dirt roads created commerce-miring mud. John Loudon McAdam (1756-1836) designed the first modern highways. He developed an inexpensive paving material of soil and stone aggregate (known as macadam), and he embanked roads a few feet higher than the surrounding terrain to cause water to drain away from the surface. At the same time, Thomas Telford, made substantial advances in the engineering of new roads and the construction of bridges, particularly, the London to Holyhead road.

Various systems had been developed over centuries to reduce bogging and dust in cities, including cobblestones and wooden paving. Tar-bound macadam (tarmac) was applied to macadam roads towards the end of the 19th century in cities such as Paris. In the early 20th century tarmac and concrete paving were extended into the countryside. Transport on roads can be roughly grouped into two categories: transportation of goods and transportation of people. In many countries licencing requirements and safety regulations ensure a separation of the two industries.

The nature of road transportation of goods depends, apart from the degree of development of the local infrastructure, on the distance the goods are transported by road, the weight and volume of the individual shipment and the type of goods transported. For short distances and light, small shipments a van or pickup truck may be used. For large shipments even if less than a full truckload (Less than truckload) a truck is more appropriate. In some countries cargo is transported by road in horse-drawn carriages, donkey carts or other non-motorized mode. Delivery services are sometimes considered a separate category from cargo transport. In many places fast food is transported on roads by various types of vehicles. For inner city delivery of small packages and documents bike couriers are quite common. People (Passengers) are transported on roads either in individual cars or automobiles or in mass transit/ public transport by bus / Coach (vehicle). Special modes of individual transport by road like rikshas or velotaxis may also be locally available.

(2) Rail Transport: Rail transport is the conveyance of passengers and goods by means of wheeled vehicles running along **railways** (**railroads**). Rail transport is part of the logistics chain, which facilitates international trade and economic growth. Typical railway tracks consist of two parallel rails, normally made of steel, secured to crossbeams, termed *sleepers* (U.K. and Australia) or *crossties* or *ties* (U.S. and Canada). The sleepers maintain a constant distance between the two rails, a measurement known as the "gauge" of the track. To maintain the alignment of the track it is either laid on a bed of ballast or secured to a solid concrete foundation. The whole is referred to as permanent way (U.K. and Australia) or right-of-way (North America).

Railway rolling stock, which is fitted with metal wheels, moves with low frictional resistance when compared with road vehicles. Locomotives and powered cars normally rely on the point of contact of the wheel with the rail for traction and adhesion (the part of the transmitted axle load that makes the wheel "adhere" to the smooth rail). This is usually sufficient under normal conditions, but adhesion can be reduced or lost through the presence of unwanted material on the rail surface, such as moisture, grease, ice or dead leaves. Rail transport is an energy-efficient and capital-intensive means of mechanised land transport and is a component of logistics. Along with various engineered components, rails constitute a large part of the permanent way. They provide smooth and hard surfaces on which the wheels of the train can roll with a minimum of friction. As an example, a typical modern wagon can hold up to 113 tonnes of freight on two four-wheel bogies or trucks. The contact area between each wheel and the rail is tiny, a strip no more than a few millimetres wide, which minimizes friction. The track distributes the weight of the train evenly, allowing significantly greater loads per axle and wheel than in road transport, leading to less wear and tear on the permanent way. This can save energy compared with other forms of transportation, such as road transport, which depends on the friction between rubber tires and the road. Trains have a small frontal area in relation to the load they are carrying, which reduces air resistance and thus energy usage, although this does not reduce the effects of side winds.

Railway tracks running through Stanhope railway station in North East England, UK Due to these benefits, rail transport is a major form of public transport in many countries. In Asia, many millions use trains as regular transport in India, China, South Korea and Japan. It is widespread in European countries. Intercity rail transport in the U.S. is relatively scarce outside the Northeast Corridor, although a number of major U.S. cities have heavily-used local rail-based passenger transport systems or light rail or commuter rail operations.

The vehicles travelling on the rails, collectively known as *rolling stock*, are arranged in a linked series of vehicles called a train, which can include a locomotive if the vehicles are not individually powered. A locomotive (or "engine") is a powered vehicle used to haul a train of unpowered vehicles. In the U.S. individual unpowered vehicles are known generically as *cars*. These may be passenger-carrying or used for freight. For passenger-carrying vehicles the term *carriage or coach* is used, while a goods or freight-carrying vehicle is known as a *freight car* in the U.S. and a *wagon* or *truck* in the U.K. An individually-powered passenger vehicle is known as a *railcar* or a *power car*; when one or more as these are coupled to one or more unpowered *trailer cars* as an inseparable unit, this is called a *railcar set* or *multiple unit*.

(3) Air Transport: Air Transport Industry is one of the best prototypes of the future world where all human activities will be integrated including administrations, companies and contractors.

Why Air transport is special: To provide its service Air Transport Industry must combine the effort of:

- people who sell the service, for instance Travel Agents;
- people who operate aircrafts, airlines;
- people who operate airports;
- traffic controllers;
- customs;
- police;

Because this service is provided across countries, it also requires the cooperation of governments. Aircrafts are one of the most blatant applications of military research to civil needs. A company that knows how to make civil aircrafts also knows how to make military aircrafts. A civil aircraft can be used to carry troops. A pilot can pilot a military aircraft. For these reasons Air Transport activities have been subsidized, protected and heavily regulated.

Aircrafts are one century old. In the first half century progress has been extremely fast with frequent breakthroughs. In the second half century progress has been much smaller. Aircraft speed did not increase; the most significant changes, wide body and turbo fans took place at the same time as the legacy organization described below. On the other hand this is only then that Air Transport changed people life.

Like computers and Internet now, aircrafts used to incarnate modernity and to trigger the same kind of passion. Air Transport did not have to be profitable. Air Transport early became a global industry requiring the cooperation of independent organizations, private companies of different size and civil servants. These organizations communicated in a B2B model well before the 2000'. Another aspect is the weight of the legacy. With so many involved countries with so different resources, interests and timetables the big bang is never an option. The Air transport system must remain compatible with 20-years old equipments. As a consequence the Air Transport system is increasingly complex and maybe the main contribution of the computers has been to enable this growing complexity. An optimal Air Transport system must combine conflicting interests like safety, low fares and noise acceptable for Airport neighbours. The involved organizations are different lifecycles. You can create a Travel Agency in a couple of days and an Airline in a couple of months but you must plan a new Airport twenty years in advance. Such a system needs regulations and the problem is to identify which regulations are needed and which regulations actually protect special interests.

(4) Sea Transport: Water transport can be broadly divided into two groups - Inland water transport and Shipping. Shipping, in turn, can again be divided into two categories Coastal shipping and Overseas shipping.

Inland Water Transportation: Inland water transport includes natural modes as navigable rivers and artificial modes such as canals. The Inland waterways have played an important role in the Indian transport system since ancient times. However, in recent times the importance of this mode of transport has declined considerably with the expansion of road and rail transport. In addition, diversion of river water for irrigation has also reduced the importance of inland water transport. The decline is also due to deforestation of hill ranges leading to erosion, accumulation of silt in rivers and failure to modernize the fleet to suit local conditions. The transportation of goods in an organized form is confined to West Bengal, Assam, parts of North Eastern region and Goa.

Development of inland water transport commenced from the Second Five Year Plan and up to the end of Fifth Plan the total expenditure on this sector was Rs. 34 crores. It was only in the Sixth Plan that this sector was given priority and specific schemes of inter-State and national importance for development of inland water transport were taken up. The Seventh Plan was an important landmark in the development of inland water transport. The expenditure on this sector in the Plan (at Rs. 131.85 crores) was more than the expenditure incurred right up to the end of the Sixth Plan. Three objectives were laid down in the Seventh Plan for the development of inland water transport.

(a) Development of inland water transport in the regions where it enjoys natural advantage.

(b) Modernizations of vessels and country crafts to suit local conditions-and

(c) Improvement in the productivity of assets. The Inland Waterway Authority has been set up which is a big step forward and should help in the accelerated development of inland water transport.

Coastal Shipping: India has a long coastline of 7,516.6 kms, a number of ports (11 major and 139 minor working ports) and a vast hinterland. Therefore coastal shipping holds a great promise more so because it is the most energy efficient and cheapest mode of transport for carriage of bulky goods like iron and steel, iron ore, coal, timber, etc. over long distances. However, despite this fact (and despite the fact that coastal shipping was reserved exclusively for Indian ships after Independence), there has been a sharp decline in coastal shipping operations. For instance, the number of ships fell from 97 in 1961 to only 56 in 1980 while Gross Registered Tonnage (GRT) fell from 3.1 lakhs to 2.5 lakhs over the same period. However, at the end of 1994 the fleet strength was 438 vessels of 6.3 million GRT. The main factors affecting the growth of coastal shipping adversely have been "High transportation costs especially for movement other than those between a pair of water front locations, port delays, poor turnaround time of coastal ships on account of overaged vessels, lack of mechanical handling, facilities etc." The coastal fleet is ageing fast; about 52 per cent of the tonnage is already overdue for replacement. Also, there is imbalance in coastal traffic movement as traffic is not equally available in both directions. This makes it necessary for coastal ships to sail in ballast, at times, on return journey. Moreover, slow handling of the cargo at port and undue port delays inflict heavy losses on shipping, companies. It is estimated that at present 70 per cent of ship time is spent at ports and only 30 per cent on voyage.

Overseas Shipping: Because of the importance of overseas shipping in international trade, considerable attention has been paid to increase the shipping tonnage in the planning period. As a result, the share of Indian shipping in the transportation of India's overseas trade has slowly and consistently increased in the planning period. From around 5 per cent in the first Plan, it increased to around 34.0 per cent at the end of 1993-94. as compared to 1.92 lakh GRT (Gross Registered Tonnage) at the time of Independence, shipping tonnage increased to 6.30 lakhs GRT in 1994.

In the First Plan Rs. 18.7 crores were spent on shipping while the expenditure in Second Plan stood at Rs. 52.7 crores. An important step taken during the Second Plan was the establishment of a non-lapsing shipping development fund for grant of loans to shipping companies for the acquisition of tonnage. The Third Plan made a provision of Rs. 55 crores for shipping which rose to Rs. 135 crores in the Fourth Plan. The Sixth Plan envisaged the augmentation of shipping tonnage for meeting increased requirements of India's foreign trade and also to replace the overaged tonnage especially the coastal vehicles. 'The outlay in this plan was kept at Rs. 720 crores while actual expenditure was only Rs. 432.94 crores. The resources constraint had forced the Seventh Plan to keep the outlay at Rs. 693.42 crores and the actual expenditure was only Rs. 670.05 crores. The broad objectives for development of shipping in this plan were kept as follows:

(a) Modernization of fleet on the basis of improved ship designed and fuel efficiency in engines.

(b) Replacement of overaged fleet on a selective basis.

(c) Drivers fixation of fleet by acquisition of cellular container ships and specialized product carriers.

(d) Addition to fleet on a selective basis, keeping in view the long-term objective of achieving- self-sufficiency in tanker fleet.

(5) Miscellaneous Modes: Besides roadways, railways and airways, liquids are transported through pipelines also. Moreover, postal services and courier services also provide facilities for transport of goods. However, these courier service agencies make use of rail, road and air transport for carrying goods. Let us discuss about courier each of these modes in detail.

Pipelines: One of the most economical means of transporting crude petroleum and oil products, natural gas and coal gas is through pipelines. Though heavy capital expenditure is involved for constructing the pipeline, the recurring expenditure to maintain it is very low. The volume and the duration of supply (long duration) of oil/gas justify the capital expenditure on construction of pipeline. Although waterways may cost less than pipelines, navigable canals and rivers are not there between many places. Thus, use of water transport for oil is restricted. There are several examples in India where pipelines are used to transport petroleum. Imported crude petroleum is transported by 1,222 Km long pipeline from Salaya in the Gulf of Kutch to Koyali and Mathura refineries via Viramgam in Gujarat. Oil wells in Naharkatiya are connected by pipelines with refineries at Nunmati in Assam and Barauni in Bihar. Coal gas is transported from Durgapur to Calcutta by pipelines.

Postal Office: Postal service undertakes transport of parcels of goods within India and abroad by surface mail or air mail. Parcels may be registered or unregistered. However for a parcel weighing 4 kg. or more, registration is compulsory. For registered parcels, acknowledgement of the consignee is also available to the sender by post. For this purpose the parcel has to be sent within 'Acknowledgement Due' and an additional amount is charged to the postage payable. Another facility provided by the postal department is the *speed post service* whereby parcels can be sent to selected destinations within and outside the country very quickly. Large post offices in the major cities of India offer this service. Postage is to be paid by the sender. Charges are very high and vary according to the weight of the parcel and destination.

High volume users are given special privileges, such as delivery under contract to any place in India, even a remote village or a far flung town. Besides, regular users can avail of the facility of scheduled pick ups from their own premises at no extra charge. Credit facility is also given to high volume users who can pay only once a month.

Advantages: Postal service, as a means of transport, has the following advantages: (1) It is a convenient means of transport where the quantity is small and the volume is low. (2) Post Offices are located mostly near market places. Hence dispatch of parcels can be arranged easily. (3) Parcels are delivered at the doorstep of the addressee's. (4) The parcel may also be sent under VPP (Value Payable Post) and the amount due from the consignee can be realized by the sender through the post office. (5) Main advantage of the speed post service is the assured and speedy delivery of goods.

Disadvantages: The disadvantages of postal services are: (1) Sending large quantities of goods by parcel post is more expensive than rail or sea transportation. (2) The maximum weight of a parcel permitted is 20 kg. The packages should not to be more than one meter long. Thus, heavy and bulky goods cannot be sent by parcel post. (3) The main disadvantages of speed post service are that it is very expensive and is available at selected places only.

Suitability: On the whole, postal service is useful for sending small quantities urgently, where such quantities are uneconomical to carry by other modes such as trucks, trains or ships. For bulky and heavy goods, parcel post or speed post are expensive and not ordinarily found suitable means of transport.

Courier Service: Many private agencies known as couriers operate from different cities and towns and undertake to carry goods to places within the country and abroad. The courier service actually involves transportation of goods by road/rail or airways. For short distances, mostly within town/city, they use messengers. Quick and assured delivery is the main advantage of courier service. It also provides the pick up service at no extra charge. The limitations of courier service are it is quite expensive and available only in cities and towns between which traffic is regular and substantial.

Q16. What are the factors to be taken in account while selecting the mode of transport?

Ans. Which mode of transport should be chosen by a business firm will depend upon the nature, weight, bulkiness and volume of goods to be transported. Generally four major factors viz., cost, speed, flexibility and regularity of the service influence the choice of a particular mode. Let us discuss these factors briefly.

Cost: The most important factor is the cost of transport. Sea transport is by far the cheapest means of transporting bulky and heavy goods, provided the speed of carriage is not an essential requirement. Rail transport is also a relatively cheaper mode of transport for heavy and bulky goods to be carried over long distances. It is also speedier than sea transport. But transport by rail is possible only when places are connected by railways. Transport by motor trucks is cheaper and speedier than rail transport for small consignments over short distances. But the cost of road transport by trucks is higher than that of rail transport for bulky goods of small value to be carried over long distances. This is due to the limited carrying capacity of trucks. Air transport is the fastest mode of transport but it is also the costliest mode. Its use is thus restricted to the carriage of perishable goods, valuable goods or spare parts of machinery urgently needed.

Speed: As regards speed of transport, motor transport by road is speedier than rail transport over short distances. But railways are potentially a speediest means than road transport for long distances. The quickest mode of transport is of course, air transport and the slowest is water transport.

Flexibility: While choosing a particular mode of transport, we have to consider the flexibility of service also. In this respect, road transport is the most flexible mode. Carriage of goods by motor trucks is possible between all places. Goods can be picked up and delivered at any point and loading as well as unloading can be arranged at any convenient time. Rail transport is relatively less flexible, as it is generally available for carriage of goods only between certain definite places. Sea transport provides services only between sea ports and to that extent is inflexible, but it is indispensable for trade between countries without common land frontiers. Air transport is also inflexible as a mode of transport. Carriage of goods is possible only between airports which are fewer and far between.

Regularity: In the case of rail transport, regularity of service is most assured. The scheduled movement of railways is relatively less affected by weather conditions. Motor trucks may or may not have scheduled services but transport by trucks is somewhat affected by bad weather conditions. Sea transport is also available according to some schedule. Only in certain parts of the world, storms and freezing of sea water may affect this mode of transport. Air transport is also available according to a fixed schedule but the services are very much affected by weather conditions.

Q17. Define warehousing. Briefly explain the types of warehousing.

Ans. A **warehouse** is a commercial building for storage of goods. Warehouses are used by manufacturers, importers, exporters, wholesalers, transport businesses, customs, etc. They are usually large plain buildings in industrial areas of cities and towns. They come equipped with loading docks to load and unload trucks; or sometimes are loaded directly from railways, airports, or seaports. They also often have cranes and forklifts for moving goods, which are usually placed on ISO standard pallets loaded into pallet racks. Some warehouses are completely automated, with no workers working inside. The pallets and product are moved with a system of automated conveyors and automated storage and retrieval machines coordinated by programmable logic controllers and computers running logistics automation software. These systems are often installed in refrigerated warehouses where temperatures are kept very cold to keep the product from spoiling, and also where land is expensive, as automated storage systems can use vertical space efficiently. These high-bay storage areas are often more than 10 meters high, with some over 20 meters high. The direction and tracking of materials in the warehouse is coordinated by the WMS, or Warehouse Management System, a database driven computer program. The WMS is used by logistics personnel to improve the efficiency of the warehouse by directing putaways and to maintain accurate inventory by recording warehouse transactions.

For a warehouse to function efficiently, the facility must be properly slotted. Effective slotting addresses which storage medium a product will be picked from (pallet rack or carton flow), and how they will be picked (pick-to-light, pick-to-voice or pick-to-paper). With a proper slotting plan, a warehouse can improve its inventory rotation requirements – such as FIFO (First In First Out) and LIFO (Last In First Out) – control labor costs and increase productivity.

Warehouse

Traditional warehousing has been declining since the last decades of the 20th century with the gradual introduction of Just In Time (JIT) techniques designed to improve the return on investment of a business by reducing in-process inventory. The JIT system promotes the delivery of product directly from the factory to the retail merchant, or from parts manufacturers directly to a large scale factory such as an automobile assembly plant, without the use of warehouses. However, with the gradual implementation of offshore outsourcing and offshoring in about the same time period, the distance between the manufacturer and the retailer (or the parts manufacturer and the industrial plant) grew considerably in many domains, necessitating at least one warehouse per country or per region in any typical supply chain for a given range of products. Recent developments in marketing have also led to the development of warehouse-style retail stores with extremely high ceilings where decorative shelving is replaced by tall heavy duty industrial racks, with the items ready for sale being placed in the bottom parts of the racks and the crated or palletized and wrapped inventory items being usually placed in the top parts. In this way the same building is used both as a retail store and a warehouse.

Modern warehouses are also used at large by exporters/manufacturers as a point of developing retail outlets in a particular region or country. This concept reduces the end cost of the product to the consumer and thus enhance the production sale ratio. Warehousing is an age old concept which can be used as sharp tool by original manufacturers to reach out directly to consumers leaving aside or bypassing importers or any other middle agencies or person.

Types of Warehouses: The warehouse is the most common type of storage though other forms do exist (e.g., storage tanks, computer server farms). Some warehouses are massive structures that simultaneously support the unloading of numerous in-bound trucks and railroad cars containing suppliers' products while at the same time loading multiple trucks for shipment to customers.

Below we discuss five types of warehouses:

• **Private Warehouse:** This type of warehouse is owned and operated by channel suppliers and resellers and used in their own distribution activity. For instance, a major retail chain may have several regional warehouses supplying their stores or a wholesaler will operate a warehouse at which it receives and distributes products.

• **Public Warehouse:** The public warehouse is essentially space that can be leased to solve short-term distribution needs. Retailers that operate their own private warehouses may occasionally seek additional storage space if their facilities have reached capacity or if they are making a special, large purchase of products. For example, retailers may order extra merchandise to prepare for in-store sales or order a large volume of a product that is offered at a low promotional price by a supplier.

(a) Automated Warehouse : With advances in computer and robotics technology many warehouses now have automated capabilities. The level of automation ranges from a small conveyor belt transporting products in a small area all the way up to a fully automated facility where only a few people are needed to handle storage activity for thousands of pounds/kilograms of product. In fact, many warehouses use machines to handle nearly all physical distribution activities such as moving product-filled pallets (i.e., platforms that hold large amounts of product) around buildings that may be several stories tall and the length of two or more football fields.

(b) Climate-Controlled Warehouse: Warehouses handle storage of many types of products including those that need special handling conditions such as freezers for storing frozen products, humidity-controlled environments for delicate products, such as produce or flowers, and dirt-free facilities for handling highly sensitive computer products.

(c) Distribution Center: There are some warehouses where product storage is considered a very temporary activity. These warehouses serve as points in the distribution system at which products are received from many suppliers and quickly shipped out to many customers. In some cases, such as with distribution centers handling perishable food (e.g., produce), most of the product enters in the early morning and is distributed by the end of the day.

Chapter-5

Government and Business

Q1. Explain the reasons underlying Government control over private business activities. **[Dec 2003, Q1(f)]**

Ans. Reasons Underlying Government Control Over Private Business :

(1) Evils of free enterprise and private ownership: The following evils are associated with free enterprise and private ownership :

- **(i)** Freedom of enterprise often gave rise to monopoly of large business firms. Monopoly power was generally used to restrict production and increase prices so as to earn higher profits.
- **(ii)** Private ownership of business has led to concentration of wealth in the hands of a few business houses. This caused wide disparities of income and wealth among the people.
- **(iii)** The growth of large companies prevented the entry of new firms in the market.
- **(iv)** For the sake of profits, private enterprises started indulging in wasteful advertisement and unfair competition.
- **(v)** Business conditions were subject to booms and depressions at periodical intervals. Depression brought about widespread unemployment and human misery. On the other hand, speculative activities during booms led to business failures and economic crisis.

(2) Establishment of welfare state: There was increasing public pressure on Government to ensure social welfare and protect the interest of the general public by controlling monopolies, establishing fair trade practices and ensuring equitable distribution of income and wealth.

(3) Planned economic development: Government intervention is necessary for rapid development of certain key industries which require large investments or which yield low returns. Besides, to take the economy in planned direction, it is also necessary to give priorities to the growth of certain industries. But, for a private entrepreneur profitability is the main consideration rather than priorities of development. Moreover, private enterprises are likely to be concentrated in certain areas where facilities are easily available. Thus backward regions in the country would be deprived of the benefit of industrial development. Therefore, for rapid economic development of the nation, government is required to regulate private business and channelise private investment in the planned direction. It is also necessary for government to directly participate in industrial and commercial activities to hasten the process of development.

(4) Other reasons: There are several other reasons which necessitate the government to regulate the private business as follows:

- **(i)** To prevent the misuse of scarce natural resources like minerals, forests, etc., by private business firms for profit.
- **(ii)** Ensuring the proper use of scarce resources keeping in view the future needs.
- **(iii)** Encouraging and protecting small-scale industries.
- **(iv)** Protection of the economy from the dominance of foreign investors.

Q2. Discuss about the instruments of Government control.

Ans. Government regulation of private business does not necessarily mean only restriction of private activities. As a matter of fact government measures of control may have inductive as well as restraining effects on business. Measures may have inductive effects if the objective is to stimulate, encourage, facilitate or induce a particular type of trade or industrial activity through technical and financial assistance, tax concessions, subsidy, bank credit, supply of foreign exchange for imports of raw materials or machinery, protection against foreign competition, etc. On the other hand, certain measures may have restraining effects if they are aimed at limiting or restricting private trade and industry by means of legal enactment and administrative orders. These may include licensing requirements for starting or expanding industries, control over capital issues, fixation of maximum price, etc. However, some of the measures may have both the effects. For example, industries which require imported raw materials may be adversely affected if imports of such raw materials are restricted or stopped. At the same time, due to such restriction on imports, the producers of competing goods may have a positive effect and earn more profit. There is another way of distinguishing between the instruments of control. Thus, controls may be classified into two categories depending on whether the measures are directly applicable or indirectly applicable. According, the two broad types of control measures may be: (1) direct controls and (2) indirect controls. Let us now discuss briefly about these two categories.

Direct Controls: Direct controls are the measures which are applied in the discretion of government authorities. Such a control may be used to promote, restrict or limit the activities of private organizations or categories thereof. Examples of these controls are:

- **(a)** Licensing of new enterprises or expansion of existing large enterprises.
- **(b)** Control over issue of shares, debentures, etc., by companies for raising capital (control of capital issues).
- **(c)** Import and export control through direct prohibition or quota

restriction.

(d) Fixing maximum or minimum prices for particular commodities.

(e) Control over distribution of commodities through rationing.

(f) Grant of subsidies for industrial growth.

(g) Incentives for export promotion like grant of subsidy, credit facilities, etc.

These controls are also known as **discretionary controls** because they involve discretions to be made by concerned government officials.

Indirect Controls: These indirect controls affect private business firms in an indirect manner. The following are some common examples of indirect controls:

(a) Changes of tax rates: Tax rates may be lowered to encourage the business or raised to discourage the business.

(b) Changes in import and export duties: Import duties may be raised so as to increase the prices of certain goods. This may be aimed at discouraging imports of those goods or to protect domestic industries from foreign competition. Import duties may be lowered to allow large imports of certain products. Similarly, export duties may be raised or lowered so as to influence the domestic demand and supply. For instance, if the export duty is raised, exports may be discouraged and domestic supply may increase to meet higher domestic demand. If it is lowered, exports may rise.

(c) Changes in interest rates on bank loans: Government can change its monetary policy to control the prices. For instance, interest rates on bank loans and credit may be raised so as to prevent excessive borrowing and expenditure by business enterprises and to reduce new investment by business firms. On the other hand, interest rates on bank loans may be reduced to induce business firms to borrow and expand their business activities.

Indirect controls are also known as **non-discretionary controls**. Government authorities do not have any discretionary power to apply the measures to particular firms and not to others in the same category.

Economic Planning: Many developing countries today have recognized the importance of planning for economic development and adopted broad economic policies for industrial growth. In India this is done through Five Year Plans. The First Five Year Plan was launched in 1951. Since then, six successive plans have been completed and the Seventh Five Year Plan is running its last year. The main objectives laid down in the plans have been:

(i) To achieve a target growth of national income so as to improve the standard of living of people.

(ii) To bring about industrial growth according to certain priorities and with particular emphasis on basic and heavy industries like steel, fuel and power, chemicals, fertilizers, engineering goods, etc. and provision of transport and communication facilities.

(iii) To generate more employment opportunities to absorb the increasing labour force.

(iv) To increase agricultural production and achieve self sufficiency in foodgrains.

(v) To reduce regional inequalities and achieve balanced regional development.

(vi) For the utilization of limited resources to the best possible advantage.

Economic planning gives a general indication of the priorities of development of various industries and accordingly guides the development process. Besides, it indicates the extent to which private organizations will be allotted scarce resources like fuel, power, finance and other facilities for growth. The economic and social activities which the government will undertake on its own are also laid down in the five year plans.

Industrial Policy : The industrial development of our country is guided, regulated, controlled and promoted according to the industrial policy. After Independence, a number of policy statements have been issued by the Government of India which define the respective roles of government, private, cooperative and joint sector organizations in industrial development. Policies also indicate the relative importance of large, medium and small-scale industrial units. In April 1948, the government adopted the first Industrial Policy Resolution, which emphasized a progressively active role of the state in industrial development. At the same time, the policy also laid down that private organizations should play a complementary role within the framework of the policy.

In 1956 the government adopted a new industrial policy resolution with the following objectives:

(i) To increase the rate of economic growth.

(ii) To speed up industrial development.

(iii) To enhance the scope of government participation in industrial growth.

(iv) To prevent private monopoly and concentration of economic power.

(v) To define the role of small, village and cottage industries.

(vi) To bring about a balanced regional development.

Under the resolution, industries were divided into three categories :

(a) Industries listed in Schedule A of the Resolution which would be developed as state monopolies. The development of these industries would be the exclusive responsibility of the state. These include atomic energy, arms and ammunition, heavy machinery, railways, air transport, etc.

(b) Industries listed in Schedule B which would be progressively state-owned and the state would generally take the initiative in establishing new units. At the same time, private enterprises would also have the opportunity to develop in the field either on its own or with state participation. The industries in this category include aluminium, drugs, machine tools, fertilizers, road and sea transport, etc.

(c) Remaining industries are those in which private organizations would take the initiative in establishing new units and expanding the existing industries.

In course of time the government modified some aspects of the policy adopted in 1956. But the basic policies remained more or less the same.

Industrial Licensing: As an instrument of government control and regulation, the system of industrial licensing was introduced to implement the Industrial Policy Resolution. Provision was made for that purpose in the Industries (Development and Regulation) Act, 1951. The Act has provided that no new industrial unit could be established or substantial expansion of existing plants made without a license from the Central Government. Further, while granting license for any new undertaking, government may lay down conditions regarding location, minimum size, etc.

The industrial licensing system was expected to achieve the following objectives :

(a) Regulation of industrial development and guiding investment in industries according to the planned priorities and targets of growth.

(b) To control monopoly and concentration of wealth.

(c) Protection of small-scale industries against undue competition from large units.

(d) Prevention of concentration of industries in few locations and secure regional decentralization of industries.

(e) Best possible use of scarce foreign exchange resources.

Q3. Why does the Government participate in business?

Ans. Government today is engaged in various types of business undertakings. There are several types of services which are provided by government organizations such as electricity, water, postal, telecommunications, transport services, etc. Besides these organizations, there are many manufacturing industries owned and managed by government. The reasons for the direct participation of government in business and industry may be divided into three categories: (1) basic reasons, (2) ideological reasons, and (3) specific reasons.

Basic Reasons: The government of India was rightly convinced that political independence without economic independence would not have much meaning. It was, therefore, decided to industrialize the country in a big way as early as possible. The government felt that if the private sector was to take the initiative, it would take an unduly long time to achieve this objective of rapid industrialization. It was so because the private enterprises lacked adequate entrepreneurship and resources to start large scale ventures. The government, therefore, made a two-pronged attack on the problem. The government encouraged private enterprises to set up new industries, but also, went into industry in a big way.

It was decided to establish steel plants, fertilizers factories and other units necessary for industrial and agricultural growth. The following is a list of some major enterprises and power projects set up by the government within a decade of Independence.

(a) Steel Plants at Rourkela, Bhilai and Durgapur
(b) Chittaranjan Locomotive Works
(c) Hindustan Machine Tools
(d) Sindri Fertiliser Factory
(e) Hindustan Shipyard
(f) Hindustan Antibiotics
(g) Hindustan Cables
(h) Integral Coach Factory
(i) Indian Telephone Industries
(j) Power and Irrigation Projects – Tungabhadra, Bhakra Nangal, Hirakud, Damodar Valley, Chambal, etc.
(k) Industrial Finance Corporation of India for providing finance to private enterprises.
(l) National Industrial Development Corporation to support industrialization in the private sector.

The intention of the government was to have economic self-reliance in as many areas and as early as possible. We have achieved this objective in a good measure.

Most of the projects set up by the government involved heavy investment, (i) long period of construction (for example, a steel plant may require five to six years), and (ii) low returns on investment. In many cases, however, there was a heavy element of risk which private enterprises, by and large, were not willing to take. The government, therefore, has played an important entrepreneurial role in industrializing the country. A large number of industries set up by the government would never have been established if we had waited for the private sector to come forward and make the necessary investment and take the risk.

Ideological Reasons: There is another side of the picture as usual. Apart from the economic and social consideration, the government had strong ideological commitment to the philosophy of public ownership of the means of production. This is the Congress Party's approach which ruled this country so far except during the brief period of 1977-79 when there was the Janata

Party Government. It is important to note that even before Independence the Congress Party committed itself to socialism through ownership of the means of production. It may be noted that the Industrial Policy Resolution of 1956 which is valid till now, has greatly and clearly emphasized the need for the government in business and this explains the importance of the government owned enterprises in Indian Economy.

Some Specific Reasons: There are many other reasons for the government to participate in business. These are specific to a particular decision. Some of these are listed below.

(a) Air Transport Business: Till 1953, there were many private air companies in the country. Most of these were financially unsound and had no money to invest in modern and costly aeroplanes. The air transport is of strategic importance to the country. The government, therefore, nationalized nine air companies and created Indian Airlines Corporation and Air India International Corporation in 1953.

(b) Insurance Business: Today, the whole of insurance business is with the government. The life insurance business is operated through the Life Insurance Corporation of India and other types of insurance business through the General Insurance Corporation of India and its four subsidiary companies.

The government went into the life insurance business in 1956 nationalizing scores of private companies which were not fulfilling the main objective of the life insurance business, namely, (i) effective mobilization of the people's savings, (ii) spreading the message of insurance as far and as wide as possible, and (iii) using the insurance funds for economic development.

Before nationalization of life insurance business in 1955, there were only 47.8 lakh policies with a total sum assured of Rs. 1,220 crores. By the end of March 1987 there were 298.8 lakh policies with a total sum assured of Rs. 60,795 crores. Moreover, funds with the Life Insurance Corporation (LIC) are invested for national development. For example, out of the total investment of Rs. 14,000 crores by the end of March 1987, Rs. 1,300 crores was given as loan to the State Electricity Boards and Rs. 561 crores for water supply and sewage schemes in the country. Over 50% of the investments are in government securities. Thus, savings of the nation are now being channelised for nationally important objectives, which was not so before nationalization. The high figures of number of policies and the sum assured also show that the message of insurance is spreading far and wide.

Similarly, the general insurance business which is now wholly run by the government companies after its nationalization in 1971, has been given the necessary social orientation. This would not have been possible had the over 100 private companies continued to run the general insurance business.

(c) Commercial Banks: The government today is in the banking business in a big way. Over 90% of commercial banking is in the hands of the government. What was the objective of the government in going into banking business? The government rightly wanted the banking system to serve the developmental needs of the economy in conformity with national policy and objectives. It also wanted the banks to have new criteria for advancing loans in order to benefit the weaker sections of the society. The private sector banks were not prepared to help the government to achieve these objectives and hence 14 major banks were nationalized in 1969 and six more banks in 1980. Earlier in 1955 the government had nationalized the Imperial Bank of India and had converted it into State Bank of India. This was done because the government's desire to open adequate number of branches in rural areas was not fulfilled by the Imperial Bank of India.

By the end of September 1987, we have 30,463 rural branches (56%) out of 54,163 branches of commercial banks as compared to 22% rural branches in 1969. Further at the end of June 1986, we find that the total advances of the nationalized banks for various agricultural activities were Rs. 9,231 crores for as many as 166 lakh accounts opened for this purpose. Similarly, loans to small scale industries were Rs. 7,836 crores in 18 lakh bank accounts.

(d) Coal Industry: The coking coal mines were nationalized in 1971. It was done because coking coal which is essential for production of iron and steel has very limited reserves in the country. The private sector was mining this fast depleting and scarce natural resources in a very wasteful manner. Other coal mines were also nationalized in 1973. The reasons for this were: (i) the private sector owners did not have the necessary funds required for increasing the coal production, (ii) the coal which is a scarce natural resources was being minded in a very unscientific way, and (iii) the private coal miners were greatly exploiting the labour employed in the mines.

(e) Oil Industry: In the 1970's the foreign oil companies Burmah Shell, Caltex and Esso were nationalized. Here the objectives was that the government should have control over a critical and strategically important resource like oil. Today, the government has full control over the production and distribution of oil. And this has paid us rich dividends in terms of self-reliance and generation of resources.

(f) Various Other Types of Business: There is yet another important reason for the government going into business of various types. Over one hundred cotton textile mills and dozens of engineering and other enterprises have been taken over by the government since Independence. This is done because the government cannot afford to lose production capacity which exists in the units which become **sick** and which the private sector wants to close down. Further, if a sick unit is closed, hundreds and thousands of employees may be out of job, which is undesirable both socially and politically.

We have listed above various nationalization measures which show the failure of private enterprises to meet the challenge of the situation. This forced the government to step into the picture. By and large, the conclusion so far is that the government in India went into business due to economic and social compulsions.

From the above discussion we can conclude the reasons for government participation in business as follows :

(a) The government's role in business in India is greatly justified by economic and social reasons.

(b) Had the government not initiated a large number of industrial activities, the Indian economy would never have got the sound base and self-reliance which it has today.

(c) A large number of enterprises have been forced on the government when they became sick and they could not be allowed to be closed down due to social and economic reasons.

(d) There is an element of ideology in the role which the government has in business today. Had the ideology not been there, the government would have disengaged itself from at least some of its business activities after completing its role as path finder or initiator.

(e) The government continues to be in business in a big way because of ideological as well as economic and social considerations.

Q4. What is Public Enterprises? Discuss about the features and objectives of Public Enterprises. [June 2005, Q1(g)]

Ans. Public Enterprises: A business organization wholly or partly owned by the state and controlled through a public authority. Some public enterprises are placed under public ownership because, for social reasons, it is thought the service or product should be provided by a state monopoly. Utilities (gas, electricity, etc.), broadcasting, telecommunications, and certain forms of transport are examples of this kind of public enterprise.

So we may conclude that it is an economic activity for which

(a) the capital is provided by the state alone or in collaboration with private sector;

(b) the management structure is provided by the state; and

(c) the operational results are exclusively borne by the state.

Features of Public Enterprise: Following are some basic features of public sector enterprises:

(a) **State Ownership and Control:** These are owned, controlled and managed by the state or public authority created for the purpose. Govt. invests the capital and thus retains ultimate control. It manages exclusively and appoints top management personnel.

(b) Financing from State Exchequer: These are financed by the State Govt. from its own exchequer. Though some of the undertakings are allowed to raise public subscriptions also. However, Govt. provides finances for them through appropriation in its budget.

(c) Service Motive: The public enterprise is set up to serve the people at large and not to earn profit at the cost of service. They do generate surplus in order to survive, compete and to accelerate the economic growth. But their main aim is to serve so that the consumers and people may be not exploited and the enterprise moves ahead smoothly and efficiently.

(d) Public Accountability : As the financing is from State Exchequer and the account books are audited by the government, therefore public enterprises are answerable to the public through its elected Parliament and State Legislature. The Parliament appoints special committees for evaluation of the policies and practices of these enterprises. These committees make necessary recommendations for the improvement of functioning etc. of these enterprises.

(e) Bureaucratic Management: Management by rules and regulations is the core of the management of public enterprises. Their operations are governed by Govt. and its employees. The management is not given complete freedom to use its resources and take policy decisions as they like. They are mainly concerned with the implementation part of the policies of the government. A business venture naturally suffers because of such set-up.

Objectives of Public Enterprise :

(a) To industrialize the nation at a faster rate.

(b) To create necessary infrastructure for smooth and balanced economic development.

(c) To help rapid economic growth.

(d) To work for surplus so as to help in self-generation of the resources for further expansion and development.

(e) To re-distribute income and wealth.

(f) To promote national and balanced regional economic development.

(g) To develop the small-scale and ancillary industries.

(h) To help achieve the import substitution thereby save and earn foreign exchange.

Q5. Comment on the contribution of private Enterprises to Indian economy.

Ans. Many people argue that if we judge the contribution of public enterprises only in financial terms, we are less than fair to them. There are many other important aspects of their contribution which cannot be ignored. Non-financial gains of public enterprises are diverse and substantial. Some of these gains are as follows :

(a) Public enterprises have a great deal for the country to emerge as an industrial nation. Today, India is considered to be among the industrialized nations of the world. We are also self-reliant in many major areas of industrial production and most items of consumer goods and services.

(b) They have helped the industrialization and development of backward areas.

(c) They have also assisted the development of backward communities, particularly scheduled castes and scheduled tribes, by providing employment opportunities.

(d) Expansion of public enterprises have led to the reduction of income disparities. As compared to private enterprises, the salary differential between the lowest and the highest paid employees is much less in public enterprises.

(e) The constitutional objective of avoidance of concentration of economic power in few hands, has been greatly achieved by the public enterprises. In the absence of these enterprises, economic power, would have gone into the hands of a few large and established business houses. It may be noted that the large business houses, which are often in the news and wild political influence, do not at present possess even one tenth of the assets owned by the public enterprises. If the industry in the hands of the government today had been with the private sector, it would have dominated the government rather than the government directing it.

(f) The dealings of public enterprises with their suppliers, dealers, customers, employees and public at large have a higher level of morality than in the counter part private enterprises.

Thus, we find that public enterprises are an important instrument in implementing the nation's social and economic policies and their success cannot and should not be measured only in terms of profit.

Q6. What are the problems associated with Public Enterprises in India? [Dec 2007, Q8(a)] [Dec 2003, Q1(h)]

Ans. The limitations of public enterprises are :

(a) Even though public enterprises are often registered as joint stock companies like any other private sector companies, their way of working is not fully commercial. It is so because these enterprises being close to the government system, often adopt the procedures, practices and attitudes prevalent in government departments.

(b) The Board of Directors of public enterprises are not fully professional. Often there is no continuity in the job of the top men.

(c) There is too much job security at all managerial levels below the board and this affects the level of performance in public enterprises.

(d) The system of reward and punishment in public enterprises more often resembles that in the government than in similar private enterprises.

(e) Many important and large public enterprises are in areas where technology is difficult and new. And also the location is not always decided from the economic point of view.

(f) The workers unions are strong and well-organised. So, they are able to extract from these enterprises more than their rightful share.

(g) Most public enterprises show poor performance due to surplus manpower and low productivity of the personnel, almost at all levels, particularly so at lower levels.

(h) Public enterprises are very large in size as compared to private enterprises. Of the first 20 largest industrial enterprises in the country (in terms of assets), not less than 16 are public enterprises. The complexity of managerial problems increase in geometric progression with increase in size. The public enterprises, by and large, have not been able to adequately cope with their complex managerial and administrative problems.

(i) Many constraints are also caused due to the public enterprises being subject to the government type audit by the Comptroller and Auditor General of India and Parliament's scrutiny of their affairs.

Q7. What are the forms of organization in Public Enterprises? What is the difference between Public corporation and Government Company?

[Dec 2007, Q7]

Ans. There are three forms of organizations in public enterprises:

(i) Departmental Organisation;

(ii) Public Corporation; and

(iii) Government Company.

(i) Departmental Organisation: When a public enterprise is organized, financed and controlled as the government department, it is known as *'departmental form of organisation'*.

(ii) Public Corporation is a corporate body created by the Parliament or State Legislature by a special Act which defines its powers, duties, functions, immunities and pattern of management. It is managed by the management committee constituted according to the provisions of the Act.

(iii) Government Company: According to the Indian Companies Act a government company is a company in which 51% or more of the total paid-up capital is held by the Central Government or any State Govt. or partly by Central Government and partly by one or more State Governments. Any company which is subsidiary of such a company is also considered a government company.

Public Corporation and Government Company

Basis of Difference	**Public Corporation**	**Government Company**
(a) Formation	Comes into existence by a special Act of Legislature.	Formed by Ministry under the Companies Act.
(b) Management	Managed by the Board of Directors nominated by the Government.	Managed by the Board of Directors plus the elected shareholders.
(c) Capital	Full funded by the Government.	At least 51% of the capital funded by the Government.
(d) Private Participation	No scope for private participation.	There is some scope of private participation.
(e) Public Accountability	Accountable to the public through legislature.	Government and the concerned ministry are accountable to the public.
(f) Operation Autonomy	Works as an autonomous body within the provisions of the Act.	Runs on commercial principles like a private enterprise and enjoys higher degree of freedom from Government interference.

Q8. Explain briefly followings : [Dec 2003, Q5]
(1) Departmental Organization (2) Public Corporation
(3) Government Company

Ans. (1) Departmental Organization: Departmental form of organization is the oldest form of organizing public enterprises. Under this form of organization, business activities of the undertakings are conducted under the overall control of one of the departments of the government. In other words, when a public enterprise is organized, financed and controlled in much the same way as any other government department, it is known as 'departmental form of organization.' This form of organization is generally, chosen for such undertakings which are important from the view point of public interest and national interest. This form is suitable for most of the undertakings which are not run on pure commercial principles. Departmental form of organization, generally, is suitable under the following situations:

(i) Where the basic purpose of an enterprise is to procure revenue for the government.

(ii) Where the government desires to have firm control over service sectors keeping in view public interest (e.g., posts and telegraph, broadcasting, etc.).

(iii) Where maintenance of secrecy is regarded as a matter of strategic importance (e.g. atomic energy, defence industries, etc.).

(iv) Where projects are in earlier stage of initial planning and require constant efforts and continuous funds that can be provided only by the government.

However, the latest trend seems to favour the participation of private enterprises even in defence industries. For instance, the Bharat Electronic Ltd., which is a state owned undertaking, is given a company form of management. A part of the telecommunication services was converted into two joint stock companies in 1981. One of them is called the Videsh Sanchar Nigam Ltd., which is responsible for the overseas telecommunication service; the other is the Mahanagar Telephone Nigam Ltd., which is responsible for telephone systems in Bombay and Delhi.

(2) Public Corporation: Public corporation is a corporate body created by the Parliament or State Legislature as the case may be, by a special Act which defines its powers, duties, functions, immunities and the pattern of management. Public corporation is also known as statutory corporation. The capital is wholly subscribed by the government. It is managed by the management committee constituted according to the provisions of the Act. It is answerable to the Parliament or State Legislature as the case may be.

As stated by Roosevelt, public corporation is an organization which is clothed with the power of the government but is possessed of the flexibility of private enterprise. Herbert Morrison views a public corporation as a combination of public ownership, public accountability and business management for public ends. Thus the public corporation device is an attempt to combine public interest with the flexibility of operation most prominently found in a company form of organization working in the private sector. Normally, the public corporations are constituted for any of the following purposes :

(i) To transfer the business of a nationalized undertaking to the corporation.

(ii) To facilitate the acquisition of undertakings belonging to an existing company.

(iii) To promote, develop and operate certain schemes.

(iv) To extend certain social services and utility services.

(v) To provide for regulation and control of the working and operations of an institution or for other matters connected therewith or incidental thereto.

The development of the public corporation is largely a post-independence phenomenon. This first public corporation was the Damodar Valley Corporation which was established under a Parliament Act in 1948. It is a multi-purpose river project. In the same year, the government set up the Industrial Finance Corporation of India to provide finance for industries in the private sector. In 1953 when the Indian Airlines and Air India were set up, the Air Corporations Act was passed. In 1955 the State Bank of India was established through the State Bank of India Act and the Life Insurance Corporation of India was set up through the Life Insurance Corporation Act of 1956. Thus, we find that whatever the government wants to undertake a commercial activity, it goes to Parliament and gets approval to set up a distinct entity.

It may be noted that it is not necessary that each corporation will have an Act of its own. More than one statutory corporation can also be established under the same act of the legislature. For example, the State Electricity Boards have been established in most of the states under the Electricity (Supply) Act of 1948. Similarly, most of the States have State Financial Corporations set up under the State Financial Corporations Act of 1951.

(3) Government Company: According to the Indian Companies Act, a government company is a company in which 51 per cent or more of the total paid-up capital is held by the central government or any state government or by many state governments or partly central government and partly by one or more state governments. Any company which is subsidiary of such a company is also considered a government company. Thus a government company is an enterprise wherein government is a predominant shareholder having the bulk of controlling interests. Government company is registered under Indian Companies Act. When the government applied to the Registrar of Joint Stock Companies for setting up a new company, it has to follow all the rules and procedures as are applicable to private persons. Just because the government is getting a company registered it does not get any concession in regard to the formal requirements.

Of late, we come across mixed-ownership companies wherein capital is jointly held by the state and private (Indian or foreign) interests. A government company in which both the government and private (enterprises/individuals) are shareholders, is known as a **mixed-ownership company**. The Government of India has registered and organized a large number of its commercial and industrial undertakings mostly as private limited companies even though their control and regulation actually rests with the government by virtue of its owning majority of shares. But why does the government do like that?

Government, normally, establishes the company form of organization for the following reasons:

(a) **Public interest:** Government sometimes acquires shares of the existing private enterprises when they are unprofitable or have become insolvent or are in financial crisis. Government acquires such companies in the interests of the country. Eastern Shipping Corporation and Hindustan Shipyard Ltd., are examples of the companies taken over by the Government of India.

(b) **Mixed-ownership:** Sometimes, in order to secure capital, technical know how, expert guidance, etc., the government may be desirous of starting an enterprise in association with private entrepreneurs. In such situations, the government may set up mixed-ownership companies. The examples of mixed-ownership companies are Hindustan Machine Tools, Hindustan Shipyard Ltd., Heavy Engineering Corporation, Hindustan Cables, etc.

(c) **Industrial promotion:** In order to encourage industrial promotion, sometimes, government may establish some companies. Such companies are not directly connected with any manufacturing activity, but they are expected to bring out commercially feasible projects to be eventually established in private or public sectors. National Industrial Development Corporation and National Small Industries Corporations are some examples in this category.

(d) **Promotion of trade or commerce:** Government may also establish some companies to promote trade or commerce. State Trading Corporation, Export Credit & Guarantee Corporation (ECGC) etc., are some examples.

(e) **Lack of incentive:** The private entrepreneur does not come forward to establish enterprises because of certain risks such as longer gestation period, heavy investment outlay, lack of profit in the initial years of its formation, etc. In such cases the government may establish government companies.

Q9. What is Public Utility? Outline the features of public utility. [Dec 2004, Q5]

Ans. ***'Public Utilities'*** are those services which are necessary to enable the smooth functions of day-to-day life of the public of an area. For example transport, electricity, health services, mail etc. In India most of these services and rendered by autonomous or semi autonomous corporations owned by State or Central Government. These autonomous or semi-autonomous bodies are called public enterprises.

Public utilities are the business undertakings engaged in supplying essential goods and for services of daily necessity for the general public. Examples of public utility services are institutions which undertake certain essential services like the supply of gas, water, electricity, urban transport etc. Thus, the business enterprises that are established to provide efficient and uninterrupted supply of the goods that are absolutely indispensable for a civilized community are referred to as public utility organizations. All the public utility undertakings have an obligation to supply the essential goods are services to everyone in the community without any discrimination at reasonable prices.

Features of Public Utilities : Following are the distinctive features of public utilities :

(a) The field of operation of public utility undertakings is mostly local.

(b) Public utilities deal with essential services such as water, gas, electricity etc. So these services are indispensable in all modern societies, thus their supply must be made regularly.

(c) Undertakings supplying essential public services by nature assume the position of a monopoly. Generally they don't have any competitors.

(d) To avoid the misuse of monopolistic position of the organizations it is essential to regulate their working as well as the price and supply policies of public utilities.

(e) Public utilities operate under franchise.

(f) Huge capital investment in fixed assets is required.

(g) The demand of public utility services is more or less inelastic. It means there will be no change in demand with rise or fall in the price of that service.

The demand of those services has been increasing day-by-day as these can't be shared.

(h) These services sell themselves. There is no need for advertisement or salesmen for creation of demand of such services.

(i) The demand of these services is non-transferable.

(j) The degree of risk involved in the business carried out by public utilities is less as compared to other industries.

Q10. Discuss about the management and organization of public utility.
[Dec 2004, Q1(h)] [June 2003, Q4(f)]

Ans. Public utility undertakings are organized in any of the following forms :

(i) Public or Private Limited Company;

(ii) Public Corporations; and

(iii) Departmental Undertakings

Every public utility undertaking has to take a license from the concerned government, which is to be renewed from time-to-time depending upon the satisfactory working of the undertaking. This license confers monopoly and franchise rights upon them. Since public interest is involved, the government has control directly or indirectly over the management and working of these undertakings.

Various Forms of Organisation and Their Management:

(1) Public or Private Limited Company:

(a) Public Limited Company : Public limited company is formed by at least seven persons. It is free from the restrictions of transferability of shares and issue of its prospectus to the public. Some examples of public limited companies are Indian Railways and Electricity Supply Undertakings.

(b) Private Limited Company: This form of organization is registered under the Companies Act, 1956, with a minimum number of the persons and maximum number of 50 persons. It has its Memorandum and Articles of Association. The important merit of this kind of organization is the maintenance of quality of product or service.

(2) Departmental Undertakings: Some public utility undertakings are run by Govt. departments under the control and direction of ministers headed by ministers. For example, Indian Post and Telegraph run by the Ministry of Communications etc. Merits of departmental undertakings are :

(a) It ensures control by responsible officials of the government,

(b) Finances are provided by the Govt.

(c) The revenue goes to the Public Exchequer,

(d) Public accountability is maintained, since report on their working is presented and discussed in Parliament/State Assembly.

(3) Public Corporations: Public Corporations are autonomous bodies set up under the special acts of Parliament or State Legislature and these derive their rights and powers through the special acts and the area of operation is also fixed by the Act. It is not completely controlled by the Govt. It works like important merits are :

(a) They possess the efficiency and flexibility of private enterprises.

(b) The broader interest of community at large is safeguarded because they are directly accountable to the Parliament/State Legislature.

Q11. How the pricing and selling strategies of public utilities are different from other organization?[June 2007, Q1(h)] [Dec 2004, Q1(h)]

Ans. The main considerations in the formulation of a proper pricing policy for public sector consist of: (1) rational allocation of resources, (2) attainment of the optimum level of operations, (3) generation of surpluses for reinvestment, (4) making products available to consumers as widely as possible, (5) coping with competition from private sector and foreign markets. The pricing policy to be adopted by a particular public enterprise depends upon several factors, e.g., (a) nature of the enterprise-industrial, public utility, promotional, regulatory, etc., (b) nature of the enterprise-industrial, public utility, promotional, etc.

In India different public enterprise have been found to follow alternative pricing policies :

(a) No-Profit-no-Loss Pricing: Under their Memorandum of Association, Hindustan Insecticides and Hindustan Antibiotics follows this price policy.

(b) Profit Pricing: Indian Railways, Sindri Fertilisers, Hindustan Machine Tools adopt this policy to contribute to public exchequer and to plough back their earnings.

(c) Subsidized Pricing: Enterprises running schemes for public welfare follow this policy, e.g., the State Bank of India Rural Branch Expansion Scheme, State Electricity Boards, Food Corporation of India.

(d) Import Parity Pricing: Hindustan Shipyard and such other enterprises follow this policy whose products have to compete with the foreign products. The landed price of imported products is considered.

(e) Concessional Pricing for long-term contract or bulk purchases: Hindustan Steel Ltd. Charges concessional prices on bulk purchases and Chittranjan Locomotives for longterm contract for the supply of locomotives.

(f) Cost plus Pricing: Hindustan Aeronautics, Indian telephone industries, Hindustan Cables and the Posts and Telegraphs Department fix prices by adding a certain margin (often 10%) of the cost of production.

(g) Dual Pricing: Under this policy higher prices are charged from rich buyers an lower prices from poor buyers.

(h) Pooled Pricing: Prices of fertilizers are fixed on the basis of the fertilizer pool. This pool comprises of retention prices paid to public sector fertilizer units and the price paid for imported fertilizers.

(i) Other practices: Some other pricing practices followed by public enterprises are as follows:

- **(1)** Enterprises like Air India, Shipping Corporation of India fix their rates as per trends in the international market. Similarly petrol prices depend on international prices of oil.
- **(2)** Enterprises with a captive market charge prices so as to generate surplus for expansion, e.g., public sector hotels.
- **(3)** STC, MMTC, etc. operate on the basis of the certain percent service charge on foreign operations.
- **(4)** The Indian Oil Corporation pays to the ONGC prices based on government award.

The ARC Study Team on Public Undertakings suggested the following criteria for price policy in public sector :

(a) Public enterprises must at least pave their way and not run into losses unless there are clear and overriding reasons on public interest as indicated in an open directive issued by the government.

(b) Public utilities and services should lay more stress upon the achievement of optimum size then upon return on investment.

(c) While determining the price structure commensurate with the surpluses expected from them, public enterprises should keep the level of output as near the rated capacity as possible, subject to the volume of demand for the products.

(d) Discriminating or differential rate pricing maybe adopted when it is observed that well-to-do people should pay more than poor ones for the same product or service.

(e) Public enterprises of industrial and manufacturing type, should as an obligation earn sufficient surplus so as to make a substantial contribution to capital formation in the country.

The ARC study team found that with the exception of those working under a system of administered prices, public enterprises in India have formulated their pricing with a view to covering costs and making a surplus on the basis of whatever assumptions they had of their financial obligations.

To be of real I have to be gentle and comprehend without interfering or creating dependence

Brahma Kumaris

QUESTION PAPERS

When I notice a weakness in another, let me also aim to recognize their strengths

Brahma Kumaris

ECO – 1: BUSINESS ORGANISATION
June, 2003

Note : Attempt all the **four** questions.

Q1. "The company form of business organisation has been successful and popular in almost all the countries." Explain.

Refer to Chapter-1, Q.No.-10

OR

(a) Explain the important features of a Joint Hindu Family.

Refer to Chapter-1, Q.No.-8

(b) Distinguish between Partner by estoppels and Partner by holding out.

Ans. Partner by estoppel : A person who behaves in the public in such a fashion as to give an impression that he is one of the partners in a partnership firm is called a partner by estoppel. Such partners are not entitled to profits but are fully liable as regards the firms obligations.

Partners by holding out: If a particular partner of a firm represents that another person is also a partner of the firm, and if such a person does not disclaim the partnership relationship even after coming to know about it, such person is called a 'partner by holding out'. Such partners are not entitled to profits but are liable as regards the obligations of the firm.

Difference between these two types is very clearly. In the case of a partner by estoppel, the person's own behavior and conduct have created a mistaken impression in the third parties mind that he is a partner of the firm. Whereas in the case of a partner by holding out, the other partners have represented the person as a partner, though he is not one, and he does not contradict it.

Q2. What is meant by underwriting? How does it help companies in raising long-term finance? State the terms and conditions relating to underwriting of shares.

Refer to Chapter-2, Q.No.-9

OR

What is meant by 'listing of securities'? What are the advantages of listing securities on a stock exchange from the point of view of the company and the investors?

Refer to Chapter-2, Q.No.-14

Q3. (a) Distinguish between Bill of Lading and Shipping Bill.

Refer to Chapter-3, Q.No.-17(i)

(b) What is a documentary bill of exchange? How does it help in securing payment of export dues from the importer?

Ans. According to Section 6 of Negotiable Instruments Act, 1881, "A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand'. From this definition, it is clear that a cheque is an instrument in writing, containing an unconditional order of a bank to pay a certain sum of money on demand to a specific person or according to his order or it may be made payable to the bearer of the instrument. There are three parties to a cheque - drawer, drawee and the payee. A drawer is the person who has an account in the bank and who is writing the cheque. A drawee is one on whom the cheque is drawn, he is liable to make the payment. In case of a cheque paying bank is the drawee. A payee is the person to whom the amount of cheque is to be paid, If the cheque is made payable to "self, the drawer himself becomes the payee. A cheque may either be a bearer cheque or an order cheque. A bearer cheque is one where the payment can be had by the person who is presenting the cheque to the bank for payment. A bearer cheque can be transferred from one person to another by mere delivery only i.e., just like cash payments. On the other hand an order cheque is one which is payable to a certain person or his order. In an order cheque, the payee must be named. An order cheque cannot be transferred from one person to another by mere delivery. It requires the endorsement of the payee. A cheque is not meant for indefinite circulation. It must be presented for payment within six months of the date appearing on the cheque. If a cheque remains in circulation for a period exceeding six months from the date of issue, it is termed as a "stale cheque" and the bank must dishonour such cheques. If a cheque bears a date which is yet to come is termed as a post-dated cheque'. A post dated cheque does not become invalid. It is valid and negotiable. But it is not payable until the arrival of the date written on it. The banks do not make the payment of a post date cheque because the written order is to be honoured on or after the date mentioned on the cheque. In order to ensure the payment by cheque absolutely safe, the cheques are crossed. Crossing of a cheque means drawing across the face of the cheque two parallel transverse lines with or without the words "And Company" between the lines. Crossing can be hand written or stamped. When a cheque is crossed, its payment cannot be received at the counter but it is always deposited in the account of the payee. The paying banker should make the payment of a cheque according to the instructions mentioned on the cheque. The paying banker should not deviate from those instructions. If the bank pays a stale cheque or pays a post dated cheque before the due date, the bank shall not receive the statutory protection. The paying banker should always make the payment in good faith and without negligence.

OR

State briefly the factors which influence the choice of the media of advertising by a business firm. List the requisites of an ideal medium of advertising.

Refer to June 2005, Q.No.-6 and Chapter-3, Q.No.-6

Q4. Answer any four of the following:

(a) Distinguish between advertising and publicity.

Refer to Chapter-3, Q.No.-1

(b) State the significance of banker's right of general lien.

Refer to Chapter-4, Q.No.-4

(c) Explain the doctrine of subrogation in respect of fire and marine insurance.

Refer to Chapter-4, Q.No.-12(ii), (iii)

(d) Discuss the usefulness of containerization for transportation of goods.

Ans. Containerisation refers to the technique of using specially made containers for transportation of goods. It involves carriage of goods in large box like containers that can be loaded and unloaded to and from trains, trucks, ships and air crafts by mechanical devices instead of manual labour being engaged in transferring packaged lots. Actually, containerisation is intended to eliminate manual handling of cargo, mechanising the operation and ensuring automatic control over transfer of goods in containers from storage to carriers and from one type of carrier to another. Containers can be hauled by trucks to railway yards, docks or airports and can be transferred readily to rakes, flatcars, ships or airplanes, the main advantage of containerisation is its adaptability to efficient transfer between different modes of transportation. The transfer can be made by mechanical devices with minimum use of manual labour. For sea transport, operation of larger and faster general cargo vessels has become possible due to containerisation. Specialised container ships are required for the purpose, and it involves heavy capital expenditure. Even then it is found economical since loading big containers is easier, less time consuming and less costly compared with loading of small boxes or pieces.

Movement of cargo by air may also be possible more conveniently with the prospect of containerisation enabling goods to be loaded and unloaded using highly automatic mechanical devices. However, it remains to be seen whether it is economically feasible to operate huge air freighters which are required to carry containerised cargo. In the West European countries and the United States, containerisation has become an integral part of the transport system. It is gradually gaining ground in India. At present Inland Container Depots (ICDs) serve as dry ports to promote exports and imports from and to inland locations. In India, presently ICDs function at seven places: Bangalore, Guntur, Anaparti, Coimbatore, New Delhi, Aimngaon (Guwhati) and Ludhiana. Besides, there is a Container Freight Station (CFS) at Patparganj in Delhi, for consolidation and dispersal of less than container load cargo. The highly computerised and automated Jawaharlal Nehru Port at Nhava Sheva is linked with the ICD at Delhi. A public sector enterprise namely Container Corporation of India was set up in 1988 under the administrative control of the Ministry of Railways. The main objective of this Corporation is to bring containerisation to hinterland, and to set up a network of ICDs and CFSs all over the country to serve as dry ports in order to promote multi-modal transport of containers between gateway ports and inland locations.

(e) How does a government company differ from a non-government company?

Ans. There are certain differences between a government companies and other joint stock companies called 'non-government companies'. They are as follows :

(1) Paid-up capital: In the case of a government company not less than 5 1% of the paid-up share capital is held by the central government or by the state government or jointly by the central or one or more state governments. There can be any combination of the shares owned by the central and state governments. But the total paid-up capital owned by one or more governments should be 5 1 % or more, to make it a government company. It may be noted that there are a few government companies which have private participation in the equity. In the case of non-government companies, major share of the paid-up capital is held by the private individual.

(2) Auditor appointment: The auditor of a government company is appointed by the government on the advice of the Controller and Auditor General of India (CAG). He is also empowered to direct the auditor about the manner and method of auditing. Sometimes, the CAG himself arise out the audit of government companies under the Companies Act. The Auditor of a non-government company is appointed .by the General Body of the company.

(3) Annual reports: The annual reports alongwith audit reports of government companies are laid before Parliament if it is a central government company, and before the state legislature in case of a state government company. In case of **a** non-government company, the audit reports are laid before its General Body.

(4) Provisions of the Companies Act: Central government has the power to exempt any provision of the Companies Act from applying to a government company except the provisions regarding audit. But, central government has nothing to do with regard to the provisions of the Companies Act relating to a non-government company.

(f) What is meant by "franchise" in relation to the operation of public utilities? Explain with examples.

Ans. The term "operation of public utilities under franchise" (hereinafter referred to as the operation under franchise) mentioned in these Regulations refers to the activity of operating certain public utilities within a special scope and period which is conducted by a franchisee of public utilities (hereinafter referred to as the franchisee) designated by Municipal Government (hereinafter referred to as the municipal government) through fair competition.

In the jurisdictional area of this municipality, the following industries that involve allocation of public resources or directly relate to public interests may be operated under franchise:

(a) the industry of water, gas or heat supply;

(b) the industry of disposing sewage or wastes;

(c) the industry of public transportation;

(d) other industries stipulated by laws and regulations.

Anyone who wants to engage in the operation under franchise shall get the corresponding franchise according to the relevant provisions.

(g) Distinguish between pool and cartel.

Ans. Pool: 'Amalgamation of the resources of the participants in an association or scheme for their common advantage, such as in making a large investment'.

A **cartel** is a formal (explicit) agreement among firms. It is a formal organization of producers that agree to coordinate prices and production. Cartels usually occur in an oligopolistic industry, where there is a small number of sellers and usually involve homogeneous products. Cartel members may agree on such matters as price fixing, total industry output, market shares, allocation of customers, allocation of territories, bid rigging, establishment of common sales agencies, and the division of profits or combination of these. The aim of such collusion is to increase individual member's profits by reducing competition. Competition laws forbid cartels. Identifying and breaking up cartels is an important part of the competition policy in most countries, although proving the existence of a cartel is rarely easy, as firms are usually not so careless as to put agreements to collude on paper.

(h) Write a short note on financial feasibility of a business.

Ans. Financial feasibility : The highest and best use of a property must be financially feasible. This means that the proposed use of a property must generate adequate revenue to justify the costs of construction plus a profit for the developer. In the case of an improved property, with obvious remaining economic life, the question of financial feasibility is somewhat irrelevant. In the case of an improved property with limited remaining economic life, the question of financial feasibility becomes a question of the maximally productive use of the site. If the value of the land As Vacant exceeds the value of the property As Improved, then redevelopment of the site becomes the maximally productive use of the property and continued use of the existing improvements that do not represent the highest net value of the site is considered to be financially unfeasible.

ECO – 1: BUSINESS ORGANISATION
December, 2003

Note: Attempt both Part A and Part B.

SECTION A

Q1. Attempt any *four* of the following :

(a) Distinguish between business and employment.

Refer to Chapter-1, Q.No.-2

(b) Write a short note on retained profits as a source of long-term finance in business.

Refer to Chapter-2, Q.No.-7(iv)

(c) Differentiate between direct and indirect channels of distribution.

Refer to Chapter-3, Q.No.-7

(d) How is risk transfer different from risk separation?

Refer to Chapter-4, Q.No.-9

(e) Write a short note on economic feasibility of business.

Ans. Determination of the likelihood that a proposed product or development will fulfill the objectives of a particular investor, called Economic feasibility. For example, a feasibility study for a proposed housing subdivision should : (1) estimate the demand for housing units in the area; (2) estimate the Absorption Rate for the project; (3) discuss legal and other considerations; (4) forecast Cash Flows; and (5) approximate investment returns likely to be produced.

Economic analysis is the most frequently used method for evaluating the effectiveness of a candidate system. More commonly known as cost/benefit analysis, the procedure is to determine the benefits and savings that are expected from a candidate system and compare them with costs. If benefits outweigh costs, then the decision is made to design and implement the system.

(f) State the reasons underlying government control over private business.

Refer to Chapter-5, Q.No.-1

(g) Differentiate between speculation and gambling.

Ans. Speculation and Gambling: One may be inclined to think that speculation and gambling are synonymous. No doubt, speculation and gambling have some common features. For instance, both depend upon uncertain happenings of the future, both involve risk of loss, and both lead to gain for someone and loss for another. In spite of these similarities, however, we can make the following distinctions.

(i) Speculation is based on foresight while gambling does not involve use of foresight.

(ii) In speculation the intention is to gain from difference in prices while gambling is purely based on betting, either winning the bet or losing it.

(iii) The risk of loss is assumed and anticipated in speculation while gambling artificially creates risk of loss.

(iv) Speculation is a rational activity, based on reasoning while gambling is a kind of blind or reckless activity.

(v) Speculation is a recognised activity, while gambling is a punishable act.

(h) State five important problems of public enterprises in India.
Refer to Chapter-5, Q.No.-6

SECTION B

*Attempt any **three** of the following :*

Q2. Explain the requisites of an ideal form of business organisation.
Refer to Chapter-1, Q.No.-12

Q3. What do you mean by underwriting of securities? How is it helpful to companies in raising long-term capital? State the terms and conditions relating to underwriting of securities.
Refer to Chapter-2, Q.No.-9

Q4. 'Advertising is a social waste.' Do you agree with this statement? Give reasons for your answer.

Ans. Advertisement is not a social waste. Advertising consists of preparing visual or oral message and their communication for making people aware of and favourably inclined towards a product or service or a point of view. The underlying objective of all advertising is to promote sales. With the mass production of goods in modern times, sales promotion inevitably requires services of mass media which can carry the advertising message to the largest possible number of potential consumers. The media of advertising thus play a vital role in the sale of goods and services. Without the use of suitable media, it is impossible to think of promoting sales in 'markets with hundreds and thousands of potential buyers. This is because salesmen can personally contact only a limited number of individuals or retail shops. Likewise, producers and traders cannot contact many people personally to pass on information relating to their products or services. Small producers and small traders may be able to sell their articles through personal approach. This method of sales promotion cannot be used in the case of mass production industries of today. Indeed growth of large scale industries and development of new methods of communication have added to the importance of advertising through different media of mass appeal like radio, television, film, etc.

The use of media not only facilitates communication of the sponsored message to the largest possible number of customers but also enables repetition of the message as often as may be necessary. This helps to reinforce the effect of advertising as well as to remind and sustain the customers interest in a product or service. Use of particular types of media makes it possible to convey information in as much detail as required by adjusting the size of the message to space or time. For example, press media (newspapers and magazines) may be used on payment of charges for as much space as needed, or radio and television may be used for advertising a product on the basis of time to be devoted. Of course, the cost of using larger space or longer time, is naturally more. Mass media (which are used for reaching the public in distant parts of a country or abroad) may thus be regarded as one of the best means of creating demand and promoting sales. Even in the case of small business firms, use of certain types of media like handbills, posters and signboards, serves the purpose of reaching many more people than is possible through personal contacts. The media used for local purposes are relatively less expensive than personal selling. Above all, media advertising provides useful support to personal selling. Salesmen and traders find it easier to impress potential customers about the usefulness or quality of products when the prospective buyers are already informed about the same through advertisements. Thus, media advertising may be regarded as complimentary to personal selling.

Q5. Differentiate between a public limited company and a government company. State the merits of government company form of organisation of public enterprises.

Refer to Chapter-5, Q.No.-8(ii), (iii)

Q6. What do you understand by outdoor media of advertising? Mention four outdoor media of advertising and explain their features briefly.

Refer to Chapter-3

Q7. Explain briefly the various types of business combinations with appropriate illustrations.

Ans. A business activity becomes a reality only when efforts are made to bring the required resources together, put them at work systematically, and coordinate their activities properly.

This is referred to as business organisation. In the opinion of J.W. Shulze, "organisation is a combination of necessary beings, materials, tools, equipment, working space apparatus and finance brought together in a systematic and effective correlation to accomplish some desired objective".

Oliver Sheldon defined it as "the process of combining the work which individuals and groups have to perform with the facilities necessary for its execution so that they provide the best channels for efficient, systematic, positive and coordinated application of the available effort".

As viewed by F.J. Wright, "organisation is the arranging or combining of resources to achieve an economic aim—either with the resources available to achieve the maximum result or profit, or to achieve a given aim with the least possible expenditure of resources".

Thus, business organisation means bringing together various components of business such as workforce, raw-materials, machines, capital, energy, etc., putting them on work systematically and coordinating and controlling their activities effectively to achieve the objective of earning profit.

Forms of Business Organisation: Business may be owned and managed by a single man, or a group of persons forming a partnership firm or as a joint stock company or even as a cooperative society.

Followings are the types of business combination:

(a) Sole proprietorship

(b) Partnership firm

(c) Company

(d) Cooperative society

The first two categories (sole proprietorship and partnership forms) may be called non-corporate forms of organisations. The remaining two categories (company form and cooperative society) may be called as corporate forms of organisations.

Entrepreneur: You know that the business is carried with the primary objective of earning profits. You also know that setting up of the business to achieve this objective requires bringing together various resources, coordinating them and controlling all activities. This has to be done by somebody who may conceive the idea of doing a particular type of business, mobilise the resources and bring the organisation into existence. Such a person who does all this is called an entrepreneur. He is the one who also bears the risk of the business. You know that although each enterprise is started with the objective of earning profit but the possibility of loss cannot be ruled out. Thus, the entrepreneur is the person who conceives the business idea., brings the organisation into existence and carry on the business activity, and prepared to bear the riskof loss.

OR

Explain the rights and duties of a bank.

Refer to Chapter-4, Q.No.-4

ECO – 1: BUSINESS ORGANISATION
December, 2004

Note: Attempt Section A and Section B both.

SECTION A

Q1. Attempt any *four* of the following:

(a) State the essential features of business as an economic activity.
Refer to Chapter-1, Q.No.-1

(b) Distinguish between trade credit and discounting of bills as sources of short-term finance.

Ans. Trade creditors: Therefore it is not a cheap source of finance. On occasions, trade credit is used is used because the buyer is not aware of the real costs involved- if he were, he might turn to other sources of trade finance. However, other forms of capital are not always available, and for a company that has borrowed as much as possible trade credit may be the only choice left. This is an important source of capital for many small companies. A company which provides credit to another is in fact putting itself in the position of a banker whose advance takes the form not of cash but of goods for which payment will be deferred. This use of trade credit between companies is extremely important from both an industrial and a national point of view.

Terms of Trade Credit: Terms of credit vary considerably from industry to industry. Theoretically, four main factors are determined the length of credit allowed.

(i) **The economic nature of the product :** Products with a high sales turnover are sold on short credit terms. If the seller is relying on a low profit margin and a high sales turnover, he cannot afford to offer customers a long time to pay.

(ii) **The financial circumstances of the seller :** If the seller's liquidity position is weak he will find it difficult to allow very much credit and will prefer an early cash settlement. If the credit term is used as part of sales promotion then, he may allow more credit days and use other means for improving liquidity position.

(iii) **The financial position of the buyer :** If the buyer is in weak liquidity position he may take long time to settle the balance. The seller may not be will to trade with such customers, but where competition is stiff there is no choice other than accepting such risk and improve on sales levels.

(iv) **Cash discounts:** when cash discounts are taken into account, the cost of capital can be surprisingly high. The higher the cash discount being offered the smaller is the period of trade discount likely to be taken.

Trade credit are also used as signalling effect on the performance of the both the buyer and the seller. Where the days allowed to customers are increasing it may indicate that the company is slipping in its debt collection and very soon may encounter cash flow problem. More days to the customers also increase the risk of bad debts which will reduce the profit levels of the company. On the other hand reducing credit days to customers may result in loss of some customers as they will always seek a supplier willing to offer more credit days. For a company, as a buyer having increased credit days may indicate that the enterprise is facing cash problems and is unable to settle their balance in good time, and this may result in loss of business. Allowing cash discounts to pass is also a cost to the business as outlined above. However, reducing the day's payment to the supplier may also indicate that the company is not trusted by its suppliers. A company with a poor track record will always face difficulties in negotiating for more days, hence the short payment period.

This the basic source of finance and many entrepreneurs do not realise that by acquiring items on credit they are obtaining short term finance. Credit just like any other source of finance has interest element hidden which most are not able to recognise. The discount may be offered to encourage early payment and the receiving company may not advantage of the discount the cost arise. Therefore it is not a cheap source of finance. On occasions, trade credit is used is used because the buyer is not aware of the real costs involved-if he were, he might turn to other sources of trade finance. However, other forms of capital are not always available, and for a company that has borrowed as much as possible trade credit may be the only choice left. This is an important source of capital for many small companies. A company which provides credit to another is in fact putting itself in the position of a banker whose advance takes the form not of cash but of goods for which payment will be deferred. This use of trade credit between companies is extremely important from both an industrial and a national point of view.

(c) Write a note on direct mail as a medium of advertising.

Ans. Direct Mail : Sending personalised letters by post to the prospective customers is a method of advertising which often pays. These communications are mostly in the form of circulars and sometimes accompanied by catalogues or price lists. The idea behind mailing circular letters is to approach the customers directly with the advertising message and to arouse his interest in the product or service with detailed explanation in a convincing manner. A mailing list is thus prepared and the litter is carefully drafted with personalised wordings. The message having a personal touch is expected to be more effective. Addressed to individual, name, the message can draw the attention of the customer without distraction from competing advertisements.

Direct mail cannot be a suitable medium for advertising products meant for public use on a mass-scale. It is best suited for products where the people to be contacted can be easily identified. For example, a company manufacturing or distributing pharmaceutical products (medicines) may easily identify the doctors or chemists for direct communication of information relating to the products. Similarly, a book publishing company may conveniently identify university teachers and send circular letters to promote the sale of its publications. But, for promoting the sale of (say) toilet soap or wrist watches, or pen direct mail is not a suitable means of advertising. It would be expensive and time consuming to undertake direct mailing of circular letters to innumerable consumers of such products who are widely scattered. Booklets, pamphlets, catalog, etc., sent by post to prospective customers also come under direct mail. These are also suitable only in the case of a selective group of customers.

(d) Explain the principles of utmost good faith and insurable interest as applicable to contracts of insurance.

Refer to Chapter-4, Q.No.-13

(e) What is the difference between horizontal combination and vertical combination of business?

Ans. Following are the differences :

(a) Nature: Under horizontal combination, units carrying on the same trade or activity join together. They operate at the same stage in the industry but in case of vertical combination, units operate at different stages of manufacture of a product.

(b) Elimination of Competition: The horizontal combination eliminates competition among the units so combined. But it is not so in vertical integration as the combined units were not competing with each other.

(c) Control over Market: Horizontal combination may lead to full control of a monopoly. But it is not so in case of vertical combination.

(d) Sell-sufficiency: Horizontal combination does not lead to self-sufficiency of materials. But in vertical integration, the manufacturer of a product may integrate with the supplier of raw material. This will lead to self-sufficiency.

(f) What are the advantages of stock exchanges from the point of view of companies?

Ans. Advantages of stock exchange from the Companies' Point of View :-

(i) Increase in the credit and goodwill of the company: Every company is not allowed to have its shares traded on the stock exchange. Permission is to be obtained by the company for getting its shares included in the list of securities to be bought and sold on the floor of the stock exchange. Before granting the permission, stock exchange authorities check whether the company is financially sound and managed by qualified people. Therefore, companies whose securities are listed are supposed to be sound companies. They enjoy better goodwill and credit in the market as compared with other companies.

(ii) Extensive markets: The securities issued by companies and other corporate bodies are quoted on the stock exchanges and are traded on the floor of the exchanges. This increases the marketability of the securities. Investors all over the world come to know about the securities and get an opportunity to invest in such securities.

(iii) Increase in the value of securities: As investors all over the world come to know about the availability of certain securities, the value of securities increases as a result of higher demand.

(iv) Knowledge about investment to the company: The companies come to know from stock exchange quotations fluctuations in the price of securities as well as the intensity of buyers' demand. While planning for raising additional capital, proper decisions can be taken whether to issue shares or debentures and about the terms of issue.

(g) Why are public enterprises organized as government companies?

Ans. Government, normally, establishes the company form of organisation for the following reasons:

(i) Public interest: Governrnent sometimes acquires shares of the existing private enterprises when they are unprofitable or have become insolvent or are in financial crisis. Government acquires such companies in the interests of the country. Eastern Shipping Corporation and Hindustan Shipyard Ltd., are examples of the companies taken over by the Government of India.

(ii) Mixed-ownership: Sometimes, in order to secure capital, technical know how, expert guidance, etc., the government may be desirous of starting an enterprise in association with private entrepreneurs. In such situations, the government may set up mixed ownership companies. The examples of mixed-ownership companies are Hindustan Machine Tools, Hindustan Shipyard Ltd., Heavy Engineering Corporation, Hindustan Cables, etc.

(iii) Industrial promotion: In order to encourage industrial promotion, sometimes, government may establish some companies. Such companies are not directly connected 'with any manufacturing activity, but they are expected to bring out commercially feasible projects to be eventually established in private or public sectors. National Industrial Development Corporation, and National Small Industries Corporation a some examples in this category.

(iv) Promotion of trade-or commerce: Government may also establish some companies lo promote trade or commerce. State Trading Corporation, Export Credit & Guarantee Corporation (ECGC), etc., are some examples.

(v) Lack of incentive: The private entrepreneur does not come forward to establish enterprises because of certain risks such as longer gestation period, heavy investment outlay, lack of profit in the initial years of its formation, etc. In such cases the government may establish government companies.

(h) State briefly why and how public utilities are regulated by the government.

Refer to Chapter-5, Q.No.-10 and Q.No.-11

SECTION B

Note: Attempt any **three** of the following :

Q2. Explain the distinctive features of co-operative organizations. State its limitations as a form of business organisation.

Refer to Chapter-1, Q.No.-11

Q3. What is meant by capital structure? Discuss briefly the factors that should be taken into account while deciding on the capital structure of a company.

Refer to Chapter-2, Q.No.-2, 3

Q4. How do the following factors influence the choice of distribution channel of a product?

(a) Nature of the product (b) Characteristics of target customers

(c) Types of middlemen

Refer to Chapter-3, Q.No.-8

Q5. What is a public utility? Discuss the main features of public utilities.

Refer to Chapter-5, Q.No.-9

Q6. Explain briefly the considerations that should be kept in view while choosing the media for advertising any product.

Refer to Chapter-3, Q.No.-6

Q7. What is a holding company? What are its advantages and drawbacks?

Ans. A **holding company** is a company that owns other companies' outstanding stock. It usually refers to a company which does not produce goods or services itself, rather its *only* purpose is owning shares of other companies. Holding companies allow the reduction of risk for the owners and can allow the ownership and control of a number of different companies. In the U.S., 80% or more of voting stock must be owned before tax consolidation benefits such as tax-free dividends can be claimed.

The following are drawbacks of the holding company :

(i) Complexity and costly managements: The management of holding company and its subsidiaries is complicated matter. All the units are managed by central authority. It requires money, time and energy to organize this form of combination so it is costly to maintain the proper control of large number of subsidiary companies.

(ii) Growth of monopoly: Holding company tries to have monopolistic control over the market. Monopoly is always considered against the interest of general public. Small industrial concern and public have to pay for the existence and efficiency of the monopolists. It thus becomes the cause of the suffering of the people and dissolution of the small business units.

(iii) Chances of fraud: There is great possibility of fraud in company transaction and preparation accounts under this arrangement. Some individuals manipulate with dishonest directors and take undue advantages of their influences.

(iv) Inefficient management: Skilled and trained hands are not available to manage the subsidiary companies. Generally the management of subsidiary is left in the hands of inefficient and incompetent persons. Therefore they are unable to perform the affairs of their business when the volume increases unduly.

(v) Exploitation: As voting powers are in the hands of the members of the holding company, they dispose of every resolution for there own interest. Thus the interest of the minority share holders is ignored and this situation exploits the subsidiaries against the holding company.

Advantages of holding company :

(i) Easy to organize: The holding is easy to organize as no legal formalities are required for its formation. A company is just to hold the majority of the shares of other companies from the market. It does not need consent of the shareholders of the subsidiary companies.

(ii) Financial benefit: The holding company can collect large amount of capital to be used for expansion and modernization of the business.

(iii) Centralized management: The subsidiary companies retain their entity. They have the additional advantage that their management is centralized which reduces the expenses of management.

(iv) Controlling output market: The holding company is in the better position to restrict production according to the market demand. It does not face problems of over production and undercutting of prices by the competing firms.

(v) Advantages of vertical integration: The holding company realizes all the advantage inherent in the vertical combination.

(vi) Allotment of territory: The holding company eliminates the competition by earmarking of market for the sale of product by each subsidiary company.

(vii) A stable combination: Holding company is a very stable form of business combination. It does not dissolve with the whims of any subsidiary company.

(viii) Business good will: The holding company with the sound financing base raises the goodwill in the market not only of its own but of the subsidiaries companies as well.

OR

"The relation between banker and customer is primarily that of debtor and creditor." Explain with suitable examples.

Refer to Chapter-4, Q.No.-3

ECO – 1: BUSINESS ORGANISATION
June, 2005

Note : Attempt both Section A and Section B.

SECTION A

Q1. Attempt any *four* of the following:

(a) Differentiate between profession and employment.

Refer to Chapter-1, Q.No.-2

(b) Write a note on cash credit as a source of short-term capital. How does it differ from bank overdraft?

Refer to Chapter-2

(c) What are the essential features of effective advertisement relating to the message?

Refer to Chapter-3, Q.No.-4

(d) How does speculation differ from investment? Give examples.

Ans. Speculation and Investment: They are two very different concepts and two different approaches to the financial markets, so even if they are often used interchangeably, it is important to be cleat about which of the two approaches to the financial markets is one taking.

A speculator is someone who seeks to buy and sell in order to take advantage of market price oscillations. An investor is someone who buys securities so that they provide a good income or capital gain by virtue of them being based on something of real and increasing worth.

Alternatively, you could say that a speculator is somebody who buys something only because they think someone else will pay more for it in the near future, as opposed to an investor, who buys it because analysis confirms that the investment is of high quality and/or good value, so it is worth holding. A speculator buys things because they expect a less informed person will buy it off them later at a higher price, whereas an investor buys things because they promise both a return on capital invested, as well as a return of capital invested.

Buyers and sellers are partly speculators and partly investors. There is a difference of degree only, Let us take the following example. A buyer agrees to purchase 100 shares at Rs. 110 per share. On the settlement date, the price goes up to Rs. 120 per share. The buyer may either ask the seller to deliver 100 shares and pay him at the rate of Rs. 110 and complete the transaction, or ask the seller to pay the difference of the two prices i.e. the price prevailing on the date of transaction (Rs.110) and the price prevailing on the date of settlement (Rs.120).

If he insists on the delivery of shares, we may call it an investment transaction. But, if he settles the transaction by taking up the difference of Rs. 10 per share, it will be called a speculative transaction. Sometimes, a person who purchased shares with the intention of investment may decide to sell the shares and reap the benefit if the price of shares goes up very high. On the other hand, if the price declines very low, he may decide to sell to avoid heavier loss. Thus, a genuine investor may also think of buying and selling securities and take advantage of changes in the prices over time. But he cannot be called a speculator because his intention is to invest and not to make profit out of changing prices.

(e) Write a short note on technical feasibility of business.

Ans. The Technical Feasibility Study assesses the details of how you will deliver a product or service (i.e., materials, labor, transportation, where your business will be located, technology needed, etc.). Think of the technical feasibility study as the logistical or tactical plan of *how* your business will produce, store, deliver, and track its products or services.

A technical feasibility study is an excellent tool for trouble-shooting and long-term planning. In some regards it serves as a flow chart of how your products and services evolve and move through your business to physically reach your market.

The Technical Feasibility Study Must Support Financial Information: Do not make the mistake of trying to entice investors with your staggering growth projections and potential returns on their investment that only includes income (revenue) to the business. With any increase in revenue there is always an increase in expenses. Expenses for technical requirements (i.e., materials and labor) should be noted in the technical feasibility study.

You should also not strictly rely on feasibility study conclusions to impress an investor. An experienced investor or lending institution will read your entire report and come to their own conclusions. Therefore, it is critical that the technical and financial data in your study reconcile. If other parts of your feasibility study shows growth, you will also have to project labor and other costs and the technical ability to support that growth.

The technical component serves as the written explanation of financial data because if offers you a place to include detailed information about why an expense has been projected high or low, or why it is even necessary. It demonstrates to potential investors and lenders (and in some cases, potential clients) that you have thought about the long-term needs your business will have as it grows.

(f) What are the advantages of listing of securities for the investor and the company?

Refer to Chapter-2, Q.No.-14

(g) State the main features of public enterprises.

Refer to Chapter-5, Q.No.-4

(h) Distinguish between Government and Non-Government Companies.

Refer to June-2003, Q.No.-4(e)

SECTION B

Note: Attempt any **three** of the following:

Q2. State the merits and limitations of partnership form of business organisation.

Refer to Chapter-1, Q.No.-7

Q3. Distinguish between investment companies and investment trusts as sources of long-term finance for companies. How can a company secure long-term finance through a leasing company?

Ans. After independence a large number of financial institutions have been established in India with the primary objective of providing long-term financial assistance to industrial enterprises. Some of these institutions have been set up on the initiative of the Central Government, while others have been set up in different states on the initiative of the concerned State Governments. Thus there are all-India institutions like Industrial Finance Corporation of India (IFCI), Industrial Credit and Investment Corporation of India (ICICT), Industrial Development Bank of India (IDBI), and Industrial Reconstruction Corporation of India (IRCI). They mainly provide long-term finance for large companies. On the other hand, at the state level there are State Financial Corporations (SFCs) and Industrial Development Corporations (SIDCs). These state level institutions mainly provide long-term finance to relatively smaller companies. These institutions (both national level and state level) are known as 'Development Banks' because their main objective is to provide financial assistance to industrial enterprises for investment projects, expansion or modernisation of plants in accordance with the priorities laid down in the Five Year Plans.

Besides the development banks, there are several other institutions known as investment companies or investment trusts which subscribe to the shares and debentures offered to the public by companies. For example, the Life Insurance Corporation of India (LIC), General Insurance Corporation of India (GIC), the Unit Trust of India (UTI), etc., come under this category. A brief account of the functions of some of these institutions is given in a subsequent section.

Investment Companies : A number of investment companies registered under the Companies Act have been engaged in financing industrial concerns by subscribing to the shares and debentures of other companies. These investment companies issue their own shares and debentures to individuals, and borrow money from other institutions. The funds so raised are invested in the shares and debentures of other companies. Besides providing long term finance to industrial concerns, the investment companies also underwrite the issue of shares and debentures of other companies. However, financing of industrial companies by the investment companies is regulated by law (the Companies Act). They can invest in the shares of another company upto 10% of the subscribed capital of that other company, and the aggregate of investments made in all other companies should not exceed 30% of the subscribed capital of the investing company. Some of the well-known investment companies in India are: Investment Corporation of India Ltd., Sri Ram Investment Co. Ltd., Eastern Investment Ltd.. Shree Sun Investment and Trading Co. Ltd., Shree Rishav Investment Co. Ltd., etc.

Investment Trusts: Another category of investment institutions which provide long-term finance to companies is investment trusts. Investment trusts specifically refer to those investment companies which are established for the investment of funds obtained from individuals and institutions. The investors receive shares (or 'units') issued by the investment trusts. These investment trusts are also known as Unit Trusts. The Unit Trust of India (UTI) is the largest organisation of this type in our country. The UTI was set up under the Unit Trust Act of 1962, and started its operation in 1964. Its initial capital was subscribed by the Reserve Bank of India, LIC, State Bank of India and other financial institutions.

Leasing Companies : Manufacturing companies can secure long-term funds from leasing companies. For this purpose a lease agreement is made whereby plant and machinery and fixed assets may be purchased by the leasing company and allowed to be used by the manufacturing concern for a specified period on payment of an annual rental. At the end of the period the manufacturing company (lessee) may have the option of purchasing the asset at a reduced price. The ownership of the asset remains with the leasing company (lessor) during the lease period. To meet its financial requirements, a manufacturing company may also sell its existing fixed assets to a leasing company at the current market price on the condition that the leasing company would ask the assets back to the seller for a specified period. Such an arrangement is known as 'sale **and** lease **back'.** The manufacturing company in this case gets the fund immediately without having to part with the physical possession of the assets. It continues to use the assets on payment of periodical rent for the lease. In any type of lease agreement, the lease rent includes an element of interest besides expenses and profits of the leasing company. Actually, the leasing company makes an investment of its own funds and must earn an income as a return on its investment through the lease rents.

Q4. Enumerate the services rendered by wholesalers to manufacturers and retailers.

Refer to Chapter-3, Q.No.-10

Q5. What is a public corporation? Explain briefly its merits and limitations.

Ans. Public corporation is corporate body created by the Parliament or State Legislature as the case may be, by a special Act which defines its powers, duties, functions, immunities and the pattern of management. Public corporation is also known as statutory corporation. The capital is wholly subscribed by the government. It is managed by the management committee constituted according to the provisions of the Act. It is answerable to the Parliament or State Legislature as the case may be.

As stated by Roosevelt, public corporation is an organisation which is clothed with the power of the government but is possessed of the flexibility of private enterprise. Herbert Morrison views a public corporation as a combination of public ownership, public accountability and business management for public ends. Thus the public corporation device is an attempt to combine public interest with the flexibility of operation most prominently found in a company form of organisation working in the private sector.'

Normally, the public corporations are constituted for any of the following purposes :

(i) To transfer the business of a nationalised undertaking to the corporation.

(ii) To facilitate the acquisition of undertakings belonging to an existing company.

(iii) To promote, develop and operate certain schemes.

(iv) To extend certain social services and utility-services.

(v) To provide for regulation and control of the working and operations of an institution or for other matters connected therewith or incidental thereto.

Merits: Public corporation strikes a mid-way between departmentally run public undertakings and the privately owned and managed corporate bodies. It absorbs some of the salient desirable features of both of them to fetch the best of both forms. At the same time, it eliminates some of their major weaknesses also. Let us discuss about the merits of a public corporation form of organisation.

(i) Initiative and flexibility: As it is an autonomous corporate body set up under an Act of legislature, it manages its affairs independently with its own initiative and flexibility. It experiments in new lines, exercises initiative in business affairs and enjoys the operational flexibility as in private enterprises.

(ii) Avoids red-tapism: The evils of red-tapism and bureaucracy associated with departmental form of organisation are avoided. Business functions cannot be carried out efficiently in a government set-up, which is marked by rules, regulations and procedures. Compared with a departmental organisation a public corporation can take quick decisions and prompt actions on any matter affecting its business.

(iii) Easy to raise capital: Public corporations are government owned statutory bodies. They can easily raise required capital on their own whenever needed by floating bonds at relatively lower rates of interest. Public also comes forward to subscribe to such bonds since they are safe.

(iv) Protects public interest: Compared to a departmental organisation, a public corporation is relatively free from political interference, parliamentary enquiry and departmental checks and controls. Although it has a considerable degree of administrative autonomy, its policies are subject to Parliamentary control. Thus, it ensures protection of public interests. Further, the Board of Directors of the public corporations consists of persons from various fields such as business experts and the representatives of special interests like labour, consumers, etc., who are nominated by the government. Thus, exploitation of any class at the cost of another is ruled out.

(v) Works with service motive: Public corporation avoids the defects of profiteering, exploitation, illegitimate speculation, etc., which are often associated with private enterprises. A public corporation works primarily with service motive and profit earning is only a secondary consideration. Though it works efficiently to show good results in the form of 'surplus,' such surplus must not be the result of exploitation. The surpluses generated by the public corporations are used for the good of the consumers and the community.

(vi) Secures working efficiency: It secures greater working efficiency by providing better amenities and more attractive terms of service to its employees which in turn; reduces the labour problems.

(vii) Secures benefits of large scale economies: Economies of large scale operations are realised by the virtue of increased size and scale of the business. Further, it is easy to reap considerable economies in management by affecting the integration of several companies under this form. For example, giant government undertakings organised as autonomous units such as, banking, insurance, transport, etc., can secure better management and staff with comparatively lesser costs.

Limitations: You have learnt about the merits of public corporation form of organisation. This form of organisation also suffers from certain limitations.

(i) Less autonomy: Compared to departmental form, public corporations enjoy more autonomy. But, in practice, the autonomy of public corporation is closely and systematically controlled by the government even in matters where they are supposed to have freedom. For example, the Food Corporation of India and the Electricity Boards in various States (these are statutory corporations) are of important to the government and to the public at large. But, the Central and State Governments often find it difficult to allow them the freedom which they are entitled to as per their Acts.

(ii) Inflexibility: A public corporation is set up by a special Act of legislature. Any change in the objects and powers of the corporation requires an amendment in the Act by the legislature. This tends to make a corporation inflexible and insensitive to changing situations.

(iii) Clash amongst divergent interests: As you know, the corporations are owned by the government and are managed by a Board of Directors appointed by the government.

When the Board of Directors represent different interests there may be clash of interests. This in turn, may hamper the smooth functioning of the corporation.

Sometimes, the directors may abuse their autonomy and authority by indulging in undesirable practices. This would defeat the social objectives of public corporation.

(iv) Ignores commercial principles: Public corporations do not have to face any competition. They are neither guided by profit motive nor haunted by the fear of loss. Therefore, there is a possibility of ignoring commercial principles in their working.

This may ultimately lead to inefficiency and losses to the corporation. The losses, thus arising are met by the government through subsidies.

(v) Excessive public accountability: You know that the public corporations work with the service motive rather than profit motive. This public accountability of the corporation sometimes acts as a stumbling block in the operational efficiency of the enterprise.

Q6. Discuss the comparative advantages of newspaper, radio and television as media for advertising any product.

Ans. Newspapers: Published in different languages, newspapers are widely and regularly read by the educated public. Reading newspaper is the daily habit 'of many people in cities and towns and some literate people in the villages. Many have also become accustomed to advertisements in newspapers and look for them as sources of information. The circulation of some of the national dailies in India runs into several millions. Newspapers published in regional languages have also wide circulation, sometimes in more than one state. Thus, as a medium of advertising, newspapers reach a very large number of people. Secondly, newspaper advertising is relatively cheaper than other media like radio and television. The space to be used can be decided in accordance with the need and cost involved. Thirdly, newspapers provide the facility of repealing the message every day, if necessary. Besides, in case of urgency, there is scope for inserting an advertisement without much loss of time. Finally, it is possible to select a particular newspaper suitable for the audience in view. For national coverage, a newspaper which has nationwide circulation can be selected. For regional coverage, a newspaper published in that regional language can be selected. Since newspapers are read by the general public, they may be used as suitable media for goods of mass consumption. Many people read the newspapers in the morning and put them aside afterwards. So, the life of the advertisement in a newspaper is short.

Radio: Broadcasting as a medium of advertising has become increasingly popular in India due to the availability of radio sets at prices which people of low income can also afford. In India radio sets are owned by a large number of population. Thus, advertisement appeals can reach the general public in different parts of the country very conveniently through radio broadcasts. In India advertisements are broadcast by the All India Radio (Vividh Bharati Programme) in specified channels. Radio Pakistan and Radio Ceylon also broadcast the advertisements for Indian population. As a mass medium, radio broadcasting is well suited for various consumer goods having a mass appeal such as movies, electric fans, refrigerators, sewing machines, leather goods, traveling bags, etc. The advantage of radio advertising is that, being an audio medium, it does not require education to receive the message. The listeners need not be literates. Besides, the message which is orally communicated may be more impressive than the message in print. The limitations of radio advertising are:

(i) it is more expensive than press advertising,

(ii) the life of the advertisement is very short, and

(iii) it is difficult to remember the message in detail.

Television : The importance of television as a medium of mass communication has significantly increased in India over the last 15 years. But its importance as a medium of advertising has grown with the use of satellite transmission and establishment of more relay stations to cover the remote parts of the country.

Individuals who cannot afford to buy TV sets are able to watch TV Programmes in community centres and public places. Use of television for advertising is increasing in recent times due to its extensive coverage and the impact of visual communication on the viewers. Its combination of sound, vision and movement permits the use of advertisement to demonstrate the product and its advantages. For this reason this medium is more effective than the press **and** radio. The major limitation of this medium is the heavy cost of advertising, particularly for advertisement before or after popular programme, known as prime time. Hence, only the large enterprises are in a position to make use of this medium.

Another limitation is that the duration of a commercial advertisement is only for a few seconds. Also viewers often find it difficult to assimilate a large number of advertisements within a short span of time.

Features of Advertising Media

	Newspaper	Radio	Television
Circulation or reach	Maximum circulation amount educated people.	Reaches large number of people	Viewers are less than the listeners of radio
Duration of attention	Very Short period of one or two-hours	For a few seconds	For a few seconds
Cost	Variable according to space	More expensive than newspapers & magazines	Most expensive
Flexibility of size, design etc.	Highly flexible	Restricted flexibility depending on available time	Restricted flexibility due to high cost & depending on available time
Suitability	Goods for mass consumption	Goods for mass consumption	Mass consumption goods

Q7. State briefly the more favourable and unfavourable outcomes of business combinations.

Refer to Dec-2003, Q.No.-7

OR

What are the rights and obligations of a bank in relation to customers? Briefly explain.

Refer to Chapter-4, Q.No.-3

ECO – 1: BUSINESS ORGANISATION
June, 2006

Note : Attempt both Section A and Section B.

SECTION A

Q1. Attempt any *four* of the following :

(a) What are the essential features of an economic activity to be termed as a business activity?

Ans. Economic Activities: These are activities which are undertaken by human beings for earning money or livelihood. These economic activities are concerned with production, exchange and distribution of goods and services. For example, a doctor working in the hospital, a teacher working in a school, an employee going to his office, a farmer working in the field, etc. Thy are all doing this to earn his or her livelihood or to acquire wealth.

We can further classify these economic activities into three groups: (a) business, (b) profession, and (c) employment.

Business: Any activity carried primarily with the object of earning profit can be called a business activity. This objective of earning profit is achieved by production and/or exchange of want satisfying goods and services. Therefore, we can define business as "any activity concerned with the production and/or exchange of want satisfying goods and services carried with a view of earning profit". Production of soaps, sale of eggs, production of TV sets, transport, etc., are some examples of business. A person who is engaged in business is called a businessman or entrepreneur. Similarly, a firm formed for the purpose of carrying a business activity is called a business enterprise or a business firm.

(b) Distinguish between Memorandum of Association and Articles of Association.

Ans. Memorandum of association : The memorandum of association of a company, often simply called the memorandum (and then often capitalised as an abbreviation for the official name, which is a proper noun and usually includes other words), is the document that governs the relationship between the company and the outside world. It is one of the documents required to incorporate a company in the United Kingdom, Ireland and India, and is also used in many of the common law jurisdictions of the Commonwealth. A memorandum of association is required to state the name of the company, the type of company (such as public limited company or private company limited by shares), the objectives of the company, its authorised share capital, and the subscribers (the original shareholders of the company). A company may alter particular parts of its memorandum at any time by a special resolution of its shareholders, provided that the amendment complies with company law. The MOA is designed to communicate to the public the state of affairs of the company and its purpose of being and operating. This aids various stakeholders of the company (creditors, suppliers, shareholders, etc.) to evaluate the extent of their risk and also possibilities of the company to overcome them at a future date.

The **articles of association** of a company, often simply referred to as the **articles** (and then often capitalised as an abbreviation for the official name, which is a proper noun and usually contains the company name), are the regulations governing the relationships between the shareholders and directors of the company, and are a requirement for the establishment of a company under the law of the United Kingdom and many other countries. Together with the memorandum of association, they form the constitution of a company. The equivalent in the United States is Articles of incorporation.

Articles of association typically cover the issuing of shares (also called stock), the different voting and dividend rights attached to different classes of share, restrictions on the transfer of shares, the rules of board meetings and shareholder meetings, and other similar issues.

In the United Kingdom, model (and default) articles of association known as Table A have been published since 1865. The articles of association of most companies – particularly small companies – are Table A, or closely derived from it. However, a company is free to incorporate under different articles of association, or to amend its articles of association at any time by a special resolution of its shareholders, provided that they meet the requirements and restrictions of the Companies Acts. Such requirements tend to be more onerous for public companies than for private ones.

The Companies Act 2006, which received Royal Assent on 8 November 2006 but will not be fully implemented until October 2009, provides for a new form of model articles of association for companies incorporated in the United Kingdom. Under the new legislation, the articles of association will become the single constitutional document for a UK company, and will subsume the role currently filled by the separate memorandum of association.

(c) Write a brief note on national depository system.

Ans. National Depository System: A depository is a central holding place, or repository, of financial securities. If transfers shares and bonds electronically, through a computer entry, and eliminates the need of investors to hold securities physically. Investors access the system through DPs, or Depository Participants – banks, brokers, mutual funds, etc. Trading ultimately becomes scriptless, as record of ownership, not physical possession, becomes the feature of trading. Transfer of ownership will be done through book entries on electronic ledgers. Transfer form sand transfer stamps will disappear.

(d) Differentiate between functional middlemen and merchant middlemen.

Ans. Middleman are usually grouped as merchants and functional middleman, according to their relations to the goods they handle. These two types are in charge of two different types of duties, the Merchant Middleman is in charge of buying the products from other buyers, while the Functional Middleman takes charge in transferring the product to their owners, but it does not have the power to do any type of usage of the product.

(e) What are the documents required for an export shipment?

Ans. When goods are exported to a foreign country, the exporter has to follow the procedure prescribed by the government. The procedure involved in exporting goods differs from country to country and depends on the existing policy of that country. The general procedure for exports from India involves the following stages:

(i) Receives enquiry
(ii) Receives and scrutinizes the order from importer
(iii) Obtains export licence
(iv) Manufactures/procures goods
(v) Fulfils exchange regulations
(vi) Books shipping space
(vii) Gets excise clearance and pre-shipment inspection
(viii) Backing and marking
(ix) Appoints clearing and forwarding agents
(x) Customs formalities
(xi) Insurance of goods and ECGC cover
(xii) Places the goods on board the ship
(xiii) Obtains bill of lading
(xiv) Collects necessary documents and despatches shipment advice to the importer
(xv) Secures payment
(xvi) Claims the incentives

Bill of Lading : A bill of lading is a document by which the shipping company acknowledges the receipt of goods on board the ship. It contains the terms and conditions on which goods are to be delivered to the port of destination. It serves as an evidence of the terms of the contract of affreightment between the exporter and the shipping company. The bill of lading is the document of title to the goods, without which goods cannot be claimed. Thus, when the goods arrive at the foreign port, the bill must be produced before they can be claimed. The bill can be made out to a certain person only, octo order, when it can be endorsed and passed on, to transfer ownership of the goods to another.

The bill of lading mentions whether the freight has been paid or yet to be paid. When the freight is paid by the exporter, the bill of lading is marked freight paid. When the freight is payable by the importer of the goods, the bill of lading is marked freightforward.

Collects Necessary Documents and Despatches Shipment Advice to the Importer. After the goods are placed on board, the forwarding agent returns the following documents to the exporter: (i) A set of 'clean on board' bill of lading, (ii) a copy of invoice duly attested by the customs authorities, (iii) copies of the shipping bill, (iv) export order in original (v) letter of credit in original (vi) duplicate copy of the AR-form and (vii) duplicate copy of GR form, as soon as the exporter receives the above documents, he sends a shipment advice to the importer, along with the following documents: (i) commercial invoice (ii) insurance policy, (iii) copies of the bill of lading which are not negotiable, and (iv) the packing list.

(f) State the components of an insurance contract.

Refer to Chapter-4, Q.No.-13

(g) State the main features of public enterprises.

Refer to Chapter-5, Q.No.-4

(h) Differentiate between merger and amalgamation.

Ans. The difference between amalgamation and merger is that in case of merger one company will be acquired or squeezed by a big company, but in case of amalgamation two or three companies will be winded up to form a new entity, here winding up of companies is done to create a new company.

Merger is a synonym word to amalgamation. Amalgamation is two or more different companies joined to form a new co.

Just like :

Co.A + Co.B = = Co.C

Absorption is a process where a company takes another company and the former company will only be there.

Just like :

Co. A ⟵ Co.B = = Co. A . i.e., Co. B is swallowed by Co. A

SECTION B

Note: Attempt any **three** of the following :

Q2. Briefly explain the factors which determine the choice of a suitable form of organisation of a business enterprise.

Refer to Chapter-1, Q.No.-13

Q3. Why do prices of securities traded on a stock exchange fluctuate? Discuss various reasons for such fluctuations.

Ans. The prices of securities, particularly those of equity shares, sometimes fluctuate very widely and critically. The changes in price take place mainly because of buying and selling activities of speculators. But underlying their speculative dealings, there are one or more other factors responsible for the price fluctuations. Generally speaking, the fluctuations are due to the following factors :

(i) Interest rate: If there is a change in the rate of interest charged by banks on loans and overdrafts, there is a change in the speculative activities, and security prices also change as a consequence of it. Thus, if banks allow credit at lower interest rate, it may induce people to borrow money from banks and engage more in speculative activities to make profits. Hence, price of securities may go up as a result of speculative buying. However, if the interest on bank credit goes up, borrowing will be reduced and demand for securities will be relatively lower. Hence prices of securities will tend to go down.

(ii) Activities of the financial institutions: When financial institutions start buying securities on a large scale, prices tend to move up because it leads to high expectation among the public about the prospects of the company and there is increased demand all around. Similarly, if there is large scale selling of securities by financial institutions, the price tends to go down.

(iii) Performance of the company: The prospects of a company as regards future profits and dividend payment are often reflected in the rising or falling prices of its shares. This is because the profit earning capacity and expected dividend rates influence the expectations of investors about the rate of return on investment and future rise in prices. If the prospects are good, there is increased demand for shares, and prices move up. On the contrary, if a company's performance in terms of profit earning and dividend payment allows an unsatisfactory trend, the price of its shares start declining due to reduced demand.

(iv) Business cycles: Business conditions are periodically found to be subject to prosperity and depression. Prices of securities continue to rise during prosperity as bull speculators are active and go on purchasing securities. However, when speculators are unable to meet their liabilities due to lack of adequate funds, they are forced to bargain for sale as a result of which prices rapidly decline and cause a state of depression in the market.

(v) Changes in Board of Directors: Sometimes, security prices change as a result of changes in the Board of Directors of particular companies. The death or resignation of a well known director may cause doubt or apprehension about the future prospects of the company concerned. In that situation, generally, there would be an adverse effect on the price of shares of that company.

(vi) Sympathetic fluctuation: The prices of securities traded in more than one stock exchange often change due to changes in another exchange. If the prices of some I securities fall in one stock exchange due to some particular reason, it leads to a decline in the prices of the same securities in other exchanges too. This happens due to immediate communication among speculators.

(vii) Political events: Changes in the composition of government, changes in international relations, conflicts and political upheavals and wars between nations are always found to cause changes in the securities prices. This is because conditions of business and industry are generally affected by political events.

(viii) Changes in government policy: The changes in government policy with regard to taxation, import-export, price controls, licensing, etc. also influence the prices of securities. For example, if government decides to exempt dividends from income tax, the share prices will go up. If, on the other hand, government decides to raise income tax rates on company profits, the prices may fall. In fact, these days the policy changes by the government have become a major cause for an upswing or a downswing in prices of shares.

Q4. You are the marketing executive of a sports goods manufacturing company. Explain various factors which you keep in mind while deciding on the channels of distribution for your products.

Ans. We can classify the distribution channels into two broad categories: (1) direct channels, and (2) indirect channels (use of middlemen).

(a) Direct Channels: When the producers sell their goods directly to the consumers it is called a direct channel. No middlemen is present between the producer and the consumer.

They establish direct link with the consumers through travelling salesmen or through their own retail shops or show-rooms. The producer or manufacturer may employ salesmen to book orders by contacting the potential users, and supply may be arranged from the stock held by the producer himself. Alternatively, the producer may set up retail shops/show rooms in different localities and sell goods directly to the customers as shown below.

Producer $\rightarrow$ Travelling Salesmen $\rightarrow$ Consumer

Producer $\rightarrow$ Retail shop/showroom $\rightarrow$ Consumer

(b) Indirect channels: In the case of all the products it is not possible for the manufacturer to supply goods directly to the consumers. So may be middlemen like wholesaler, retailer and mercantile agents may be engaged in the channel of distribution. When the middlemen are engaged, it is called an indirect channel. As shown below, there could be four indirect channels.

Producer $\rightarrow$ Retailer $\rightarrow$ Consumer

Producer $\rightarrow$ Wholesaler $\rightarrow$ Consumer

Producer $\rightarrow$ Wholesaler $\rightarrow$ Retailer $\rightarrow$ Consumer

Producer $\rightarrow$ Agent $\rightarrow$ Wholesaler $\rightarrow$ Retailer $\rightarrow$ Consumer

Channels of Distribution Used for Consumer Goods: Sports goods are consumed by the consumers so they are called consumer goods. Under this category you can find a very wide range of items such as food items, stationery, cars, clothing, shoes, household electrical appliances, TV sets, transistors, etc. The channel of distribution used for different products are not the same. Channels are different from one type of product to the other.

As shown in the figure, sometimes consumers go directly to the factory and buy the goods or order the goods from the catalogue. Durable consumer goods like cars, clothing, furniture, textbooks, shoes, etc., are generally distributed through retailer. In many cases showrooms are established by the manufacturer himself which undertake the retail trade. For example, Bata Shoe Company sells shoes through its showrooms. Consumer goods like auto spare parts, stereos, video recorder, etc., are distributed through wholesalers and retailers.

Consumer goods of daily need like foodgrains, sugar, salt, edible oil, soap, paper, pencils, etc., are generally distributed through agent or broker, wholesaler and retailer.

Q5. "The relationship between a banker and its customer is primarily that of a debtor and creditor." Comment.

Refer to Chapter-4, Q.No.-3

OR

Explain the circumstances which lead to the formation of business combinations.

Refer to Dec-2003, Q.No.-7

Q6. Compare the statutory corporation and company form of organisation of public enterprises. Which of these two do you recommend for managing public enterprises? Give reasons.

Ans.

Basic	Public Corporation	Government Company
Formation	Comes into existence by a special Act of legislature.	Formed by ministry under the companies Act.
Legal Status	It is a separate legal entity.	It is a separate legal entity.
Management	Managed by the Board of Directors nominated by the government	Managed by the Board of Directors consisting of members nominated by the government plus the elected shareholders.
Capital	Fully subscribed by the government	Minimum of 51% by the government.
Scope for Private Participation	No scope for private participation	Scope for private national/ international participation in its share capital and hence in its affairs too.
Operational Autonomy	Works as an autonomous body within the provisions of the Act, Enjoys considerable degree of antonym as there is no government interference in day-to-day affairs.	Runs on commercial principles like a private enterprises and enjoys higher degree of freedom from government interference.
Flexibility	Subject to some restrictions by the government. Not subject to budged, audit and accounting procedures of the govt.	More freedom from government control. Not subject to audit budget and accounting procedures of the government.
Public Accountability	Accountable to the public through legislature.	Government and the concerned ministry is accountable to the public.
Operating finance and Borrowing powers	Makes own arrangements and enjoys borrowing powers. It has authority to use its revenues.	Makes own arrangements and enjoys borrowing powers, it has the authority to use the revenue.
Staffing and Terms of Service	Employees are not civil servants. Employees governed by its own contract of service.	Employees are not civil servants. Employees governed by its own contract of service.

Q7. "Expenditure on advertising is an economic waste." Comment.

Refer to Chapter-3, Q.No.-3

ECO – 1: BUSINESS ORGANISATION
December, 2006

Note : Attempt both Section A and Section B.

SECTION A

Q1. Attempt any *four* of the following :

(a) Distinguish between company form and co-operative form of business organizations.

Ans. Company form of Organisation: For large scale business, you require large investment and specialized managerial skills. The element of risk is also very high. This situation led to the emergence of company form of business organisation. In case of joint stock company, capital is contributed by not one or two persons but by a number of persons called shareholders. Thus, it is possible to raise large amount of capital. A joint stock company is an association of persons registered under Companies Act for carrying on some business. It is called an artificial person as it is created by law, with a distinctive name, a common seal and perpetual succession of members. It can sue and be sued in its own name. The most widely quoted definition of a company (called Corporation in USA) is the one given by Chief Justice Marshal. According to him "a corporation is an artificial being, invisible, intangible and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or an incidental to its very existence." Lord Justice Lindley has defined it as "an association of many persons, who contribute money or money's worth to a common stock and employ it for a common purpose. The common stock so contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are members. The proportion of capital to which each member is entitled is his share."

The Indian Companies Act (1956) defines joint stock company as "a company limited by shares having a permanent paid up or nominal share capital of fixed amount divided into shares, also of fixed amount, held and transferable as stock and formed on the principles of having in its members only the holders of those shares or stocks and no other persons."

Cooperative form of Organisation: Cooperative organizations are generally started by the poor and the economically weak sections to promote their common economic interests through business propositions. The basic philosophy of cooperative organization is self-help and mutual help. The primary objective of any cooperative organization is to render service to its members. In this respect, it is different from the other three forms of organizations which are primarily meant for making profits. The important features of the cooperative organization are service in place of profit, mutual help in place of competition, self-help in place of dependence and moral solidarity in place of unethical business practices.

(b) Briefly explain the relationship between a banker and the customer.

Refer to Chapter-4, Q.No.-3

(c) Differentiate between trade association and chamber of commerce.

Ans. An **industry trade group**, also known as a **trade association**, is an organization founded and funded by businesses that operate in a specific industry. An industry association participates in public relations activities such as advertising, education, political donations, lobbying and publishing, but its main focus is collaboration between companies, or standardization. Associations may offer other services, such as producing conferences, networking or charitable events or offering classes or educational materials. Many associations are non-profit organizations governed by bylaws and directed by officers who are also members. In countries with a social market economy, the role of industry trade groups is often taken by employers' organizations which also have a role in the social dialogue.

A **chamber of commerce** (also referred to in some circles as a **board of trade**) is a form of business network. Business owners in towns and cities form these local societies to advocate on behalf of the business community. Local businesses are members, and they elect a board of directors or executive council to set policy for the chamber. The board or council then hires a President, CEO or Executive Director, plus staffing appropriate to size, to run the organization.

Generally, chambers of commerce serve the following purposes :

- Creating a strong local economy
- Promoting the community
- Providing networking opportunities
- Speaking with government on behalf of business
- Political action, such as getting pro-business candidates elected to office

In some areas, Chambers may serve other purposes, such as arbitrating disputes between business or serving as a "Better Business Bureau," but this is not generally the case. The first chambers of commerce were founded in 1599 in continental Europe (Marseille, France and Brugge, Belgium). The world's oldest English-speaking chamber of commerce is that of Glasgow, Scotland, which was established in 1783.

(d) Write a short note on underwriting.

Refer to Chapter-2, Q.No.-9

(e) Differentiate between speculation and gambling.
Refer to Dec-2003, Q.No.-1(g)

(f) How is advertising different from publicity?
Refer to Chapter-3, Q.No.-1

(g) Differentiate between a wholesaler and a retailer.

Ans. Wholesaler : Wholesalers are those who happen to **he** engaged in wholesaling or wholesale trade. In a broad sense, any individual or business firm, selling goods in relatively large quantities to buyers other than the ultimate consumers may be called a wholesaler. Thus manufacturers who sell their products directly to retailers may be regarded as wholesalers. However in a more specific sense the term wholesaler may be defined as a merchant middleman engaged in buying and reselling of goods to retailers another merchants or to industrial or commercial users. Wholesalers do not sell the products to ultimate consumers. The wholesalers belong to the category of merchant middlemen who acquire title to the goods they handle. Agents or brokers may also act as wholesale middlemen but they do not acquire the title to goods. Wholesalers act as middlemen between producers or importers of goods on [he one hand, and retailers or industrial users on the other. The goods traded by Wholesalers may include agricultural commodities, forest products, minerals as well as manufactured goods.

Retailing : Retailing refers to all transactions which involve sale of goods to the ultimate consumers for personal consumption. If the buyer uses the goods for reselling purposes it will not be treated as a retailing transaction. Any individual or business unit or shop primarily engaged in retail selling is known as a retailer or retail store. In a general sense, even a manufacturer or wholesaler may sometimes engage in sale of goods to the ultimate consumers. But they are not called retailers as retailing is not the major activity of a manufacturer or wholesaler. Thus a retailer or retail store is one whose business consists primarily of sale of goods to consumers for their own use, but not for resale in business. Retail business may include other types of transactions also. It will be treated as a retailing business if more than half of its total sales revenue is from retail trading.

A retailer is a middleman because retailing involves procuring goods from suppliers (generally wholesalers) and selling them to consumers for their personal use. Retailers perform the very important task of making goods available to consumers, which after all is the objective that underlies the production of goods. Retailers thus form a vital link in the channel of distribution of products.

(h) Distinguish between a public corporation and a government company.

Ans.

Basic	Public Corporation	Government Company
Formation	Comes into existence by a special Act of legislature.	Formed by ministry under the companies Act.
Legal Status	It is a separate legal entity.	It is a separate legal entity.
Management	Managed by the Board of Directors nominated by the government	Managed by the Board of Directors consisting of members nominated by the government plus the elected shareholders.
Capital	Fully subscribed by the government	Minimum of 51% by the government.
Scope for Private Participation	No scope for private participation	Scope for private national/ international participation in its share capital and hence in its affairs too.
Operational Autonomy	Works as an autonomous body within the provisions of the Act, Enjoys considerable degree of antonym as there is no government interference in day-to-day affairs.	Runs on commercial principles like a private enterprises and enjoys higher degree of freedom from government interference.
Flexibility	Subject to some restrictions by the government. Not subject to budged, audit and accounting procedures of the govt.	More freedom from government control. Not subject to audit budget and accounting procedures of the government.
Public Accountability	Accountable to the public through legislature.	Government and the concerned ministry is accountable to the public.
Operating finance and Borrowing powers	Makes own arrangements and enjoys borrowing powers. It has authority to use its revenues.	Makes own arrangements and enjoys borrowing powers, it has the authority to use the revenue.
Staffing and Terms of Service	Employees are not civil servants. Employees governed by its own contract of service.	Employees are not civil servants. Employees governed by its own contract of service.

SECTION B

Note: Attempt any **three** of the following :

Q2. What do you understand by commerce? Briefly explain the classification of commerce with suitable examples.

Refer to Chapter-1, Q.No.-4

Q3. What is capital structure? Why does capital structure differ from company to company?

Refer to Chapter-2, Q.No.-2

Q4. Explain the procedure you have to follow while importing goods.

Refer to Chapter-3, Q.No.-16

Q5. What are the factors to be taken into consideration while choosing a suitable medium of advertising?

Ans. The ultimate purpose of advertisement is to induce the customers and influence them to buy the goods and services. To be effective, the advertisement must have right type of message communicated through prop& media so as to reach the right people at the right time and at the lowest cost possible. Designing an effective advertisement is a challenging task. There is no definite formula for that purpose. But certain guidelines may be kept in view while designing an advertisement. The essential characteristics of a good advertisement may be divided into two broad categories:

(1) Features relating to the message

(2) Features relating to consumer reach

(1) Features Relating to the Message: The impact of an advertisement depends not only upon what is said about the product, but also how it is said. The message should be such as to win the attention and interest of the target audience. So, while designing the advertisement message, one should keep the following points in mind.

(a) Desirability: The message should say something desirable and interesting about the product. Otherwise, the advertisement may fail to induce the customers to buy the product.

(b) Exclusive: Customers should know how the Product advertised is better than the other products. So, the advertisement message should point out the unique features of the product. In other word;, it should say something exclusive or distinctive about the product which does not apply to any other brand in that product category. Then only people may realise why and how the product is better than others.

(c) Believable: Whatever is stated in the message should be believable. For instance, if the message conveys imaginary qualities of any product, people will never take the advertisement seriously. The message should actually compare with the product which the customer may verify so as to be convinced. Therefore, the message should be believable and provable.

(d) Attractive: If the message is attractive, it will draw the attention of the customers very easily. If the message is not catchy, it will not have any effect on the minds of people. Therefore, such words or pictures which may draw the attention of customers should be used in the advertisement.

(e) Memorable and easy to recall: The message should be easy to remember, so that it may be easy to recall it. Whenever customers go for shopping, the advertisement message should come to their mind and remind them about the product. Therefore, the words used in the message should be easy to rnemorise and recall.

(2) Features Relating to Consumer Reach: Apart from the message, the impact of an advertisement also depends on how well it reaches the target customers. For this purpose, the following points should be borne in mind while designing the advertisement.

(a) Appropriate media: The advertisement message should be presented through the media to which the target customers have access. For example, if the majority of the target customers do not have television sets, the message presented by TV transmission will not reach them. Similarly, if the majority of customers are illiterate, the message presented in newspapers may not reach them. So, the use of appropriate media is highly important for the effectiveness of advertisements.

(b) Frequency: Frequency refers to the number of times any advertisement is repeated within a specified period of time. It also refers to the time gap between two or more advertisements. In other words, it refers to how many times and at what intervals the advertisement is repeated. The main purpose of repetition is to keep the message alive in the memory of the customers. If the frequency is less, people may not remember the message. If the frequency is more, people may get irritated and may stop giving attention to it. So, the frequency should be optimum.

(c) Timing: The specific time of advertising the message is an equally important aspect of advertisement. For example, if the advertisement appears on the T.V. when most of the customers are not viewing it, the effect will be much less as compared with the effect when a majority of the customers are viewing the T.V. programme. Hence, the timing of the advertisement should be so determined that it may reach the majority of customer.

Q6. What is business risk? Explain the process of risk management.

Refer to Chapter-4, Q.No.-9, 10

OR

What are the different forms of business combinations? Explain any two of them in detail.

Refer to Dec-2003, Q.No.-7

Q7. What is a public utility undertaking? State its essential features.

Refer to Chapter-5, Q.No.-9

ECO – 1: BUSINESS ORGANISATION
June, 2007

Note: Attempt both Part A and Part B.

SECTION A

Q1. Attempt any four of the following :

(a) State the characteristics of an entrepreneur.

Refer to Chapter-1, Q.No.-14

(b) Differentiate between insurable risks and non-insurable risks.

Refer to Dec-2007, Q.No.-1(d)

(c) Write a short note on commercial feasibility of business.

Ans. Feasibility reports are prepared to examine the feasibility of the business in a systematic manner. Feasibility reports are prepared by experts and cover different aspects of the business. All these reports together give a clear idea about the future conditions in which the business has to operate. Feasibility of a business venture can be examined from different angles. These are :

(a) Technical Feasibility;
(b) Economic Feasibility:
(c) Financial Feasibility;
(d) Commercial Feasibility; and
(e) Managerial Feasibility.

(a) Technical Feasibility: Technical feasibility involves detailed examination of the following three aspects of the business:

(i) Location of the Plant or Factory: It is the most basic consideration. Deciding on the most advantageous location requires consideration of alternative sites. Availability of essential services and supplies such as power, labour, raw materials must be considered before finalizing the location of the plant/factory.

(ii) Size of Plant/Factory: The size of plant/factory depends upon two things (i) the size of the market; (ii) the optimum size of the plant.

(iii) Technical Requirements of the Factory: It is the most important factor to be considered. Technical feasibility of the factory/plant can be assured, if up-to-date technology is used and there is efficiency of production from the point of view of cost and quality of output.

(b) Economic Feasibility: It is generally based on market analysis of the product. The following points are to be considered to ascertain the economic feasibility:

(i) The Size of the Market: It can be ascertained on the basis of market research and market survey of the product.

(ii) Project growth in the market.

(iii) The market share expected to be captured.

(c) Financial Feasibility: The study of financial feasibility starts with the calculations of the initial costs of setting up the business. This includes cost of site development, roads, installation of machinery etc. Financial feasibility of a business depends not only on profit earned, but also to a greater extent on its ability to meet the current and future liabilities.

(d) Commercial Feasibility: Commercial feasibility of a business depends on several factors like potential demand for the product, cost of production, distribution, administration and the intensity of competition from producers of similar or substitute products. In other words, determination of commercial feasibility requires the estimation of operating costs and projection of the selling price keeping in view the nature of competition which may prevail over time.

(e) Managerial Feasibility: Last but not the least, efficiency and skills of the people, who run the business are very much important for the success of the business. Non-availability of skilled management way lead to big loss, wastage and failure of business. Thus, the feasibility of a business from the managerial point of view must be examined properly.

(d) Differentiate between ownership capital and borrowed capital.

Ans. Ownership Capital: The amount of capital invested in a business by its owners is known as **Ownership Capital**. It is on the basis of their investment that owners become entitled to the profits of the business. In a business under sole proprietorship, the individual owner normally invests capital from his own savings. In a partnership business, each partner contributes capital as mutually agreed among partners. Companies raise capital by issuing shares. Investors who contribute towards the share capital of a company become its owners by virtue of their share holding. They are entitled to receive dividend out of the profits earned by the company. The owners cannot claim to get any return on their investment unless there is profit. The rate of return on owners investment depends on the level of profits earned. If there is no profit, the owners go without any dividend. The risk of losses and of low rates of return are, thus, associated with ownership capital. Hence it is known as 'risk capital'.

Ownership capital may be used for financing fixed assets as well as continuous investment in current assets. Ownership capital is generally used as permanent capital or long-term capital. As risk-bearers, owners do not have any assurance whether they will get adequate returns on their investment or not. But they receive high returns if the business is successful. Besides, owners have a right to participate in the management of the business. A sole proprietor as also the partners of a business play an active part in running the business. Shareholders of companies do not manage the business directly. They elect members of the Board of Directors who manage the affairs of the company on behalf of the shareholders.

Borrowed Capital: The financial requirements of the business are often met by raising loans. Loans carry a certain fixed rate of interest which must be paid at regular intervals, half-yearly or yearly. There is also a commitment that the principal amount will be repaid in due course. Thus, if loan is raised for a period of 10, 15 or 20 years, its repayment may fall due at the end of that period or after stated intervals according to the terms on which the loan has been raised. Interest on loan is a fixed expense which has to be paid irrespective of the income. Thus, borrowing of money involves fixed obligation to pay interest and repay the principal amount as and when due.

Money may be borrowed for short-term and long-term purposes i.e., to finance fixed assets as well as current assets. In a sole proprietary business the proprietor can borrow money on his personal security or on the security of his existing assets. A partnership firm can raise loans on the personal security of the individual partners whereby they become jointly and severally liable. Companies can also borrow either by issuing debentures or bonds or raise direct loans.

If business income is stable and cash is realised from debtors regularly, raising of loan is not difficult. But if conditions are such that payment of interest is not possible as and when due, serious consequences may follow. There is loss of credit worthiness, that is, suppliers may not be prepared any more to supply materials on credit, further loans may not be forthcoming and lenders and creditors may even start legal action to recover their dues. Hence, borrowing money without the ability to meet the obligations of paying interest and repaying the principal is not desirable.

(e) What is securities depository system?

Ans. In the depository system, securities are held in depository accounts, which is more or less similar to holding funds in bank accounts. Transfer of ownership of securities is done through simple account transfers. This method does away with all the risks and hassles normally associated with paperwork. Consequently, the cost of transacting in a depository environment is considerably lower as compared to transacting in certificates Promoters / Shareholders National Securities Depository Limited (NSDL), the first depository in India. This depository promoted by institutions of national stature responsible for economic development of the country has since established a national infrastructure of international standards that handles most of the securities held and settled in dematerialised form in the Indian capital market. Using innovative and flexible technology systems, NSDL works to support the investors and brokers in the capital market of the country. NSDL aims at ensuring the safety and soundness of Indian marketplaces by developing settlement solutions that increase efficiency, minimise risk and reduce costs. At NSDL, we play a quiet but central role in developing products and services that will continue to nurture the growing needs of the financial services industry.

(f) 'Advertising is a social waste.' Comment.

Refer to June-2006, Q.No.-7

(g) Differentiate between functional middlemen and merchant middlemen.

Refer to June-2006, Q.No.-1(d)

(h) Briefly comment on the pricing policy of public utility undertakings.

Refer to Chapter-5, Q.No.-11

SECTION B

Note : Attempt any **three** of the following.

Q2. What is a joint stock company? Explain how it overcomes the limitations of partnership form of business organisation.

Refer to Chapter-1

Q3. Why do prices of securities fluctuate in the stock exchange?

Refer to June-2006, Q.No.-3

Q4. Explain the advantages and problems of foreign trade for the economic development of a country.

Ans. First Refer to Chapter-3, Q.No.-14

Problems in Foreign Trade: Because of cultural and other environmental differences between various countries and the distance involved, foreign trade involves certain problems which do not arise in connection with home trade. Let us examine these problems in detail.

(a) Suitability of the product for the market: Securing information about the suitability of products in the foreign market is a challenging task for every international marketer. This involves heavy expenditure and requires special skill and knowledge. Besides, the quality and price of goods must be more attractive as compared with similar products manufactured abroad. This requires intensive market research on the potential sale of goods to be exported.

(b) Changes in supply and demand conditions: International markets are often subject to changes in the supply and demand for particular products due to the entry of new competitors or increased competition of local producers or because of changes in buyers' preferences. These changes cannot be easily anticipated by the exporters.

(c) Frequent price changes: The price of products in the international market may be affected by different factors. The changes may be due to changes in exchange rates of the currencies of importing and exporting countries, higher import duties or freight rates. These factors increase the risks of foreign trade a great deal.

(d) Credit risk: International trade which is generally on a large scale involves heavy amounts to be paid by the importer. The exporters often sell their products on credit and therefore have to bear the credit risk arising from the buyer's default, bankruptcy etc.

(e) Changes in exchange rate: An additional risk of foreign trade is the risk of changes in exchange rates. The rate at which the currency of importing countries can be converted into the currency of exporter may cause losses to the exporter or the importer.

(f) Rules, regulations and procedures: Every country imposes certain restrictions in the export and import of goods to protect its economic and political interests. Besides, the rules and regulations differ from country to country and are changed from time to time. For example, the provisions of Imports and Exports Control Act, 1947 changes in export import policy and the restrictions on trade often create complications and problems for importers and exporters.

(g) Credit worthiness of importer and reliability of exporters: The value of goods involved in external trade is fairly high and the exporter has to grant credit facilities to the importer. Since there is no direct contact between exporter and importer, it is necessary that the exporter must take steps to verify the credit worthiness of the importer and importer should check the reliability of the exporter for supply of goods. This may take a long time and cause delay in the availability of goods.

(h) Transportation and cargo risks: International trade takes place either by land, air or water transport and goods have to be transported over long distances. Water transport occupies a predominant place in transporting goods across the national boundaries because ships can carry large volumes of cargo at low cost. In spite of all developments in transportation, the risks of loss or damage to cargo by fire, storm, collision, leakage, explosion, spoilage etc. exist.

(i) Time gap: The distance involved is usually greater in transporting goods from one country to another country and hence the transit time is longer.

This time *gap* involves exporter's capital being locked up over a long period.

(j) Political and legal problems: Political risks may arise as a result of changes in governments or capture of cargo by enemies etc. Commercial laws may be different between the trading countries. Moreover, conducting legal proceedings in a foreign country is complicated and expensive.

Q5. Outline the factors which you keep in mind while deciding channels of distribution for your product.

Refer to Dec-2004, Q.No.-6

Q6. Explain various modes of creating charge by banks while lending.

Refer to Chapter-4, Q.No.-8

OR

Explain the circumstances which lead to the formation of business combinations.

Refer to Dec-2003, Q.No.-7

Q7. What is a public enterprise? State the features and objectives of public enterprises.

Refer to June-2008, Q.No.-7

ECO – 1: BUSINESS ORGANISATION
December, 2007

Note: Attempt both Part A and Part B.

SECTION A

Q1. Distinguish between any two of the following:
(a) Public Limited Company and Private Limited Company
Ans.

Basis of Comparison	Private Limited Company	Public Limited Company
Formation	Difficult due to legal formalities	Quite difficult due to many legal formalities
Specific regulation	Companies Act, 1956	Companies Act, 1956
Legal status	Separate legal status	Separate legal status
Membership	Minimum 2 and maximum 50	Minimum 7 and no maximum limit
Capital	Larger capital resources	Any amount of capital can be raised
Management and ownership	Control risk and ownership generally go together	Complete separation of management from ownership
Managerial expertise	Scope for expertise	Very wide scope for expertise
Owner's liability	Limited	Limited
Basis of profit sharing	Shared by owners in the proportion of shares held	Shard by owners in the proportions of shares held
Ownership transfer	Restricted and relatively difficult	At will and very easy
Business stability	Perpetual existence, Death, insolvency of the members does not effect the life	Perpetual existence, death insolvency of the members does not effect the life
Business secrets	Secrets shared by the members	Exposed to public
State regulations	Considerable regulations	Excessive regulations
Tax liability	Heavily taxed and income is double taxed	Heavily taxed and income is double taxed.
Flexibility	It is an elastic organisation	It is unelastic organisation. Its memorandum of Association is difficult to change. It can be changed through the permission of the Govt.
Auditing of Accounts	Compulsory	Compulsory
Winding up	Under the Act	Under the Act

(b) Fixed Capital and Working Capital

Ans. Fixed Capital is a concept in economics and accounting, first theoretically analysed in some depth by the economist David Ricardo. It refers to any kind of real or physical capital (fixed asset) that is not used up in the production of a product and is contrasted with circulating capital such as raw materials, operating expenses and the like. Fixed capital is that portion of the total capital that is invested in fixed assets (such as land, buildings, vehicles and equipment) that stay in the business almost permanently.

Refining the distinction between fixed and circulating capital in Das Kapital, Karl Marx emphasizes that it is really purely relative, i.e. refers only to the comparative rotation speeds (turnover time) of different types of capital assets. Fixed capital also "circulates", except that the circulation time is much longer, because a fixed asset may be held for 5, 10 or 20 years before it has yielded its value and is discarded for its salvage value.

In national accounts, fixed capital is conventionally defined as the stock of tangible, durable fixed assets owned or used by resident enterprises for more than one year. This includes plant, machinery, vehicles & equipment, the value of land improvements, and buildings. Land itself is not included in fixed capital even though it is a fixed asset, because it is not a product (a reproducible good). But the value of land improvements is included.

Attempts have been made to estimate the value of the stock of fixed capital for the whole economy using direct enterprise surveys of "book value", administrative business records, tax assessments, and data on gross fixed capital formation, price inflation and depreciation schedules. A pioneer in this area was the economist Simon Kuznets.

Working Capital, also known as **net working capital**, is a financial metric which represents operating liquidity available to a business. Along with fixed assets such as plant and equipment, working capital is considered a part of operating capital. It is calculated as current assets minus current liabilities. If current assets are less than current liabilities, an entity has a **working capital deficiency**, also called a **working capital deficit**.

A company can be endowed with assets and profitability but short of liquidity if its assets cannot readily be converted into cash. Positive working capital is required to ensure that a firm is able to continue its operations and that it has sufficient funds to satisfy both maturing short-term debt and upcoming operational expenses. The management of working capital involves managing inventories, accounts receivable and payable and cash.

(c) Advertising and Publicity

Refer to Chapter-3, Q.No.-1

(d) Insurable risks and Non-insurable risks

Refer to Chapter-4, Q.No.-11

Q2. Write short notes on any two of the following:

(a) Entrepreneurship development

Refer to Chapter-1, Q.No.-14

(b) Underwriting

Refer to Chapter-2, Q.No.-9

(c) Importance of foreign trade

Refer to Chapter-3, Q.No.-14

(d) Essentials of a good transport system

Ans. A good transport system is one which should serve the purpose of transportation and satisfy the following requirements.

(i) It should be ***economical.*** The cost of transport service should be low enough to enable the users to carry their goods at the lowest possible charge so that the ultimate consumer get the products at a reasonable price.

(ii) It should be capable of ***carrying goods as speedily as possible.*** There should not be any delay in reaching the destination except for natural calamities or unavoidable causes.

(iii) The transport service should be ***available regularly*** as and when required. It must ensure the safety of the goods.

(iv) It should be ***operated*** by ***the properly skilled and efficient*** persons capable of handling problems in emergency.

(v) It should provide ***for insuring the risks of loss*** or damage to goods in transit, and assure payment of due compensation in case of delay causing loss to the owner of goods.

(vi) There should be ***proper arrangements for loading and unloading*** of goods promptly and at minimum cost.

(vii) As far as possible, ***delivery*** of ***goods should be made at locations*** convenience to the receiver of the goods.

SECTION B

Note: Attempt any **three** of the following :

Q3. Explain the features of an ideal form of business organisation.

Refer to Chapter-1

Q4. What is a stock exchange? Explain the primary functions of stock exchanges.

Refer to Chapter-2, Q.No.-10

Q5. Explain very briefly the procedure to be followed while exporting goods from India.

Ans. When goods are exported to a foreign country, the exporter has to follow the procedure prescribed by the government. The procedure involved in exporting goods differs from country to country and depends on the existing policy of that country. The general procedure for exports from India involves the following stages:

(i) Receives enquiry
(ii) Receives and scrutinizes the order from importer
(iii) Obtains export licence
(iv) Manufactures/procures goods
(v) Fulfils exchange regulations
(vi) Books shipping space
(vii) Gets excise clearance and pre-shipment inspection
(viii) Backing and marking
(ix) Appoints clearing and forwarding agents
(x) Customs formalities
(xi) Insurance of goods and ECGC cover
(xii) Places the goods on board the ship
(xiii) Obtains bill of lading
(xiv) Collects necessary documents and despatches shipment advice to the importer
(xv) Secures payment
(xvi) Claims the incentives

Q6. Explain the duties and rights of a banker towards the customers.

Refer to Chapter-4, Q.No.-3

Q7. What are the forms of organisation in public enterprises? Describe the features of each form.

Refer to Chapter-5, Q.No.-7 and Q.No.-8

Q8. (a) State the problems of public enterprises in India.

Refer to Chapter-5, Q.No.-6

(b) State the features of a good advertisement message.

Refer to Chapter-3, Q.No.-4

ECO – 1: BUSINESS ORGANISATION
June, 2008

Note: Attempt both Part A and Part B.

SECTION A

Q1. Distinguish between any *two* of the following:

(a) Industry and Commerce

Refer to Chapter-1, Q.No.-3 and Q.No.-4

(b) Bulls and Bears

Ans. Bull or Long: A person who buys securities in the expectation of a rise in their prices, is called 'Bull'. He becomes active whenever there is anticipation of a rise in the prices of securities. He buys with the object of selling them in future. He is also known as tejiwala. If his expectations come true, he earns a profit. If the market goes against his expectation, he incurs a loss. Suppose, he makes a deal for purchase of 100 shares at Rs. 105, expecting it will go up. On the settlement day the price of the share rises to Rs. 110. He informs his broker to settle the deal. He earns a profit of Rs. 500. On the other hand, if the market price of the share goes down he may incur a loss on settlement of the transaction. In such a situation he can postpone the settlement due to unfavourable price by paying budla charges (also called contango). He is called 'bull' as he has a tendency to raise the price artificially like a bull who generally throws his victim upwards.

Bear: A person who sells short i.e., sells what he does not possess at the time of selling, is called a 'Bear'. He does so in the hope of buying at a lower price at the time of delivery. Thus a bear anticipating a fall in price in future sells at the current price which is high. If his expectations come true, he gains, otherwise he loses. If the market goes against him i.e. if the market prices rise, he can postpone his settlement by paying badla charges (also called backwardation). A sale of securities by bears is called 'short selling'. He has to buy them from the market for making delivery to the buyer.

(c) Wholesaler and Retailer

Refer to Chapter-3, Q.No.-10 and Q.No.-12

(d) Pledge and Hypothecation

Refer to Chapter-4, Q.No.-8

Q2. Write short notes on any *two* of the following:

(a) Memorandum of Association

Ans. Memorandum of Association: It is the most important document of a company as it lays down the constitution of the company and states the relationship of the company with the outside world. It is a public document and each person who deals with the company is supposed to know the provisions contained in the memorandum. The purpose of memorandum is to enable the shareholder, creditors and those who deal with the company to know what is its permitted range of activities. Although the company is a legal 'person' its capacity to do business, unlike that of a real person, is restricted. If a company is engaged in any trade or business which is outside the provisions of the Memorandum of Association, such acts are regarded ultra vireos of the company and therefore, void and inoperative.

The Memorandum of Association contains the following particulars under different clauses :

(i) Name of the company

(ii) Name of the state in which the registered office is to be located.

(iii) **Objects clause:** The nature of business activities which the company will undertake is to be stated in this clause.

(iv) A declaration that the liability of' the members will be limited to the face value of shares subscribed.

(v) **Capital clause:** The total amount of capital with which the company is proposed to be registered and its divisions into different shares of a fixed amount are to be stated under this clause.

(vi) A declaration by signatories to the Memorandum that they are desirous of being formed into a company and agree to take the number of shares mentioned against their names.

(b) Retained profits as a source of finance

Ans. Retained Profits: An important source of long-term finance for ongoing profitable companies is the amount of profit which is accumulated as general reserve from year to year. To the extent profits are not distributed as dividend to the shareholders, the retained amount can be reinvested for expansion or diversification of business activities. It can also be used for renovation of assets or modernization of plant and equipment. It may be interpreted that the existing shareholders provide the finance. Hence, the company must decide to reinvest profits only when the rate of return is comparable with that of other similar companies. Moreover, a part of the profits must be distributed as dividend keeping in mind shareholders' expectation and the effect of dividend rate on the market price of shares. Retained profit is an internal source of finance. Hence, it does not involve any cost of floatation, which has to be incurred to raise finance from external sources. Further, the company does not have to face the uncertainties of external financing. The only drawback of this source of long-term finance is that it depends on the availability of adequate profits for retention.

(c) Features of an ideal medium of advertising
Refer to Chapter-3, Q.No.-4

(d) Containerisation
Ans. Refer Q4(d), Page No.-152

SECTION B

Attempt any **three** of the following questions.

Q3. "Partnership form of business organizations emerged essentially because of the limitations and failures of the sole proprietorship organizations." Discuss.
Refer to Chapter-1, Q.No.-7

Q4. Explain various methods of raising short term capital.
Refer to Chapter-2, Q.No.-4

Q5. Explain various factors to be kept in mind while deciding on channels of distribution for a product.
Refer to Chapter-3, Q.No.-8

Q6. What is insurance? Explain various legal aspects of insurance.
Refer to Chapter-4, Q.No.-11

Q7. What is a public enterprise? How is it different from private enterprise? Explain the characteristics of a public enterprise.

Ans. A business organization wholly or partly owned by the state and controlled through a public authority. Some public enterprises are placed under public ownership because, for social reasons, it is thought the service or product should be provided by a state monopoly. Utilities (gas, electricity, etc.), broadcasting, telecommunications, and certain forms of transport are examples of this kind of public enterprise.

Difference Between a Public Enterprise and a Private Enterprise: Private enterprises, on the other hand, refer to industrial and commercial organisations which are set up under individual or group ownership within the general framework of regulatory laws and rules of the government. These include manufacturing and commercial companies, medium and small firms organised as proprietory and partnership concerns.

Private enterprises are primarily motivated by private profit. Public enterprises are governed by public policies framed by governrnent and aimed at maximising social welfare and upholding public interest. The objectives of public enterprises in India are laid down in conformity with the objectives of the development plans. They are accountable to the government and the parliament or state legislatures regarding the fulfillment of their objectives. Private enterprises are free to set their objectives and to undertake any business activity except those, which are illegal. However, private enterprises are also regulated by government controls of different kinds.

The main characteristics of public enterprises as distinguished from private enterprises are as follows :

(a) Public enterprises are owned and managed by the govemment or agencies set up by the government.

(b) The whole or major part of the capital required for the public enterprises is provided by government.

(c) A public enterprise can be organised as a departmental undertaking or as a statutory corporation or as a government company.

(d) These are governed by public policies laid down by the government in the public interest and are not entirely guided by profit motive.

(e) Their objectives are laid down in conformity with the development plans. They are accountable to the Parliament or state legislature for their performance and fulfillment of objectives.

Q8. (a) "Expenditure on advertising is a social waste." Comment.

Refer to Dec-2003, Q.No.-4

(b) State the main features of a public corporation.

Refer to Chapter-5, Q.No.-8(ii)

ECO – 1: BUSINESS ORGANISATION
December, 2008

Note: Attempt both Part A and Part B.

SECTION A

Q1. Attempt any four of the following :

(a) State the main features of company form of organisation.
Refer to June 2006, Q.No.-6

(b) Enumerate any five functions of an entrepreneur.
Refer to Chapter-1, Q.No.-15

(c) What do you understand by bank overdraft and cash credit facilities as a source of short-term finance?
Refer to Chapter-4, Q.No.-2

(d) Explain the concept of 'underwriting' of securities.
Refer to Dec 2006, Q.No.-1(d)

(e) What are the advantages of listing of securities on a stock exchange ?
Refer to June 2003, Q.No.-2

(f) Distinguish between 'Advertising' and 'Publicity.
Refer to June 2003, Q.No.-4(a)

(g) Briefly explain the nature of banker's right of general lien.
Refer to June 2003, Q.No.-4(b)

(h) Comment on the sales policy of public utility undertakings.
Refer to Chapter-5, Q.No.-11

SECTION B

Attempt any three of the following :

Q2. What are the special features of a cooperative form of organisation? Explain its merits and limitations.
Refer to Chapter-1, Q.No.-11

Q3. Describe the role of an entrepreneur in business promotion. How does an entrepreneur differ from a promoter?

First : Refer to Chapter-1, Q.No.-14, 15

Economics, however, always did and still does use the term "entrepreneur" in a sense other than that attached to it in the imaginary construction of functional distribution i.e., in relation to capitalists, landowners, and laborers. It also calls entrepreneurs those who are especially eager to profit from adjusting production to the expected changes in conditions, those who have more initiative, more venturesomeness, and a quicker eye than the crowd, the pushing and promoting pioneers of economic improvement. This notion is narrower than the concept of the entrepreneur as used in the construction of the functional distribution; it does not include many instances which the latter includes. It is awkward that the same term should be used to signify two different notions. It would have been more expedient to employ another term for this second notion for instance, the term "promoter." The promoter concept refers to a datum that is a general characteristic of human nature, that is present in all market transactions and marks them profoundly. This is the fact that various individuals do not react to a change in conditions with the same quickness and in the same way. The driving force of the market, the element tending toward unceasing innovation and improvement, is provided by the restlessness of the promoter and his eagerness to make profits as large as possible.

Q4. What do you mean by capital structure? Explain the factors determining the capital structure of a firm.

Refer to Dec 2004, Q.No.-3

Q5. Explain briefly the importance of stock exchange in a modern society and state its shortcomings.

Refer to Chapter-2, Q.No.-10

Q6. 'Advertisement is a waste'. Comment.

Refer to Dec 2003, Q.No.-4

OR

Discuss the factors which influence the choice of distribution channel.

Refer to Chapter-3, Q.No.-8

Q7. What is insurance? Explain various types of insurance.

Refer to June 2008, Q.No.-6

ECO-1: BUSINESS ORGANISATION
June, 2009

Note : Attempt both Section-A and Section-B.

SECTION A

Q1. Attempt any four of the following
(a)State the main features of partnership form of organization.

(b) Enumerate the documents to be filed for the registration of a company. Explain briefly the nature and purpose of any one of these documents.

(c) Distinguish between insurable risk and non-insurable risks.

(d) Explain any five factors determining capital structure.

(e) explain the concept of preference shares and its advantages as a method of raising long-term finance.

(f)What is speculation? State its merits.

(g) How are the advertisements harmful to society? Explain briefly.

(h) Explain the nature and purpose of various types of warehouses.

SECTION B

Attempt any three of the following questions:

Q2. Who is termed as an entrepreneur? Explain the role of entrepreneur in business promotion.

Q3. What do you understand by the term 'development bank'? describe the functions of any three major development banks in India.

Q4. Define stock exchange. Enumerate the factors affecting prices in a stock exchange.

Q5. Explain briefly the features of an ideal advertising medium, and state the factors to be taken into consideration while choosing a suitable medium.

Q6. What is meant by business risk? Explain the main causes due to which business risks may arise.

OR

Discuss the merits and limitations of public corporation as a form of organization for public enterprises.

Q7. Discuss the various aspects of price policy of public utilities.

ECO-1: BUSINESS ORGANISATION
December, 2009

Note : Attempt both Section-A and Section-B.

SECTION A

Q1. Distinguish between *any two* of the following.

(a) Company form of business organization and cooperative society form of business organization.

Refer to December-2006, Q.No.-1(a)

(b) Ownership capital and borrowed capital.

Refer to June-2007, Q.No.-1(d)

(c) Departmental store and super market.

Refer to Chapter-3, Q.No.-13[1, 3]

(d) Insurable risks and Non-insurable risks.

Refer to December-2007, Q.No.-1(d)

Q2. Write short notes on *any two* of the following:

(a) Pricing policy of public utilities.

Refer to June-2007, Q.No.-1(h)

(b) Any five primary functions of stock exchanges.

Refer to December-2007, Q.No.-4

(c) Direct mail as a medium of advertising.

Refer to December-2004, Q.No.-1(c)

(d) Bank overdraft as a method of short-term finance.

Refer to Chapter-4, Q.No.-2, Page No.-93

SECTION B

Attempt any three of the following questions:

Q3. Define the term business ? Explain its features and objectives.

Refer to Chapter-1, Q.No.-1

Q4. Explain various methods of raising long term capital.

Refer to Chapter-2, Q.No.-4

Q5. State the features of an ideal medium of advertising. Explain briefly the various media of advertising and suggest which of them is ideal in all respects.

Refer to June-2003, Q.No.-3(b)

Q6. "The relationship between a banker and the customer is primarily that of a debtor and creditor." Discuss.

Refer to Chapter-4, Q.No.-3,

Q7. Compare the Departmental form of organization in public enterprises with statutory corporation form of organization. Which of these two forms would you prefer for managing public enterprises and why?

Refer to Chapter-5, Q.No.-8

Q8. (a) What are the essentials of a good transport systems?

Refer to December-2007, Q.No.-2(d)

(b) Write a short note on 'aids to trade'.

Refer to Page No.-5[Aids to trade]

ECO-1: BUSINESS ORGANISATION
June, 2010

Note : Attempt both Section-A and Section-B.

SECTION A

Q1. Distinguish between *any two* of the following :

(a) Business and Trade

Refer to Chapter-1, Q.No.-4

(b) Rights issue and Public issue of shares

A rights issue is an issue of additional shares by a company to raise capital under a seasoned equity offering. The rights issue is a special form of shelf offering or shelf registration. With the issued rights, existing shareholders have the privilege to buy a specified number of new shares from the firm at a specified price within a specified time. A rights issue is in contrast to an initial public offering, where shares are issued to the general public through market exchanges. **Public issue of shares or** an initial public offering (IPO), referred to simply as an "offering" or "flotation", is when a company (called the issuer) issues common stock or shares to the public for the first time. They are often issued by smaller, younger companies seeking capital to expand, but can also be done by large privately owned companies looking to become publicly traded.

(c) Advertisement and Publicity

Refer to Chapter-3, Q.No.-1

(d) Pledge and Hypothecation

Refer to Chapter-4, Q.No.-8

Q2. Write short notes on *any two* of the following:

(a) Underwriting

Refer to Chapter-2, Q.No.-9

(b) Partnership deed

Refer to Chapter-1, Q.No.-9

(c) Direct channels of distribution

Refer to Chapter-3, Q.No.-7

(d) Warehousing

Refer to Chapter-4, Q.No.-17

SECTION B

Attempt any three of the following questions:

Q3. "Company form of business organizations merged essentially because of the limitations and failures of the partnership form of business organizations." Discuss.

Refer to June-2003, Q.No.-1

Q4. What do you understand by capital structure? If you promote a car manufacturing company, what factors do you keep in mind while deciding on the capital structure of your company?

Refer to Chapter-2, Q.No.-2

Q5. "Different channels of distribution are used for different products."

Ans. Types of distribution:

Three types of distribution can be used to make product available to consumers: (1) intensive distribution, (2) selective distribution and (3) exclusive distribution. In intensive distribution, the product is sold to as many appropriate retailers or wholesalers as possible. Intensive distribution is appropriate for products such as chewing gum, candy bars, soft drinks, bread, film, and cigarettes where the primary factor influencing the purchase decision is convenience. Industrial products that may require intensive distribution include pencils, paperclips, transparent tape, file folders, typing paper, transparency masters, screws, and nails. In selective distribution, the number of outlets that may carry a product is limited, but not to the extent of exclusive dealing. By carefully selecting wholesalers or retailers, the manufacturer can concentrate on potentially profitable accounts and develop solid working relationships to ensure that the product is properly merchandised. The producer also may restrict the number of retail outlets if the product requires specialized servicing or sales support. Selective distribution may be used for product categories such as clothing, appliances, televisions, stereo equipment, home furnishings, and sports equipment. When a single outlet is given an exclusive franchise to sell the product in a geographic area, the arrangement is referred to as exclusive distribution. Products such as specially automobiles, some major appliances, certain brands of furniture, and lines of clothing that enjoy a high degree of brand loyally are likely to be distributed on an exclusive basis. This is particularly true if the consumer is willing to overcome the inconvenience of traveling some distance to obtain the product. Usually, exclusive distribution is undertaken when the manufacturer desires more aggressive selling on the part of the wholesaler or retailer, or when channel control is important, exclusive distribution may enhance the product's image and enable the firm to charge higher retail prices. Sometimes manufacturers use multiple brands in order to offer exclusive distribution to more than one retailer or distributor. Exclusive distribution occurs more frequently at the wholesale level than at the retail level. In general, exclusive distribution lends itself to direct channels (manufacturer to retailer). Intensive distribution is more likely to involve indirect channels with two or more intermediaries.

Q6. "All business risks are not insurable." In the light of this statement, explain insurable risks and non-insurable risks.

Refer to Chapter-4, Q.No.-11

Q7. Why is it considered necessary for the government to directly participate in business and industry?

Refer to Chapter-5, Q.No.-3

Q8. (a) Why do the prices of securities traded on a stock exchange fluctuate widely?

Refer to June-2006, Q.No.-3

(b) "Foreign trade is an engine of economic growth in a country". Comment.

Refer to Chapter-3, Q.No.-14

ECO-1: BUSINESS ORGANISATION
December, 2010

Note: Attempt both Section-A and Section-B.

SECTION A

Q1. Attempt any four of the following:

(a) Distinguish between business and profession.

(b) Outline the main features of sole trader organization.

(c) Enumerate the various methods of raising short term capital.

(d) What are the main sources of foreign funds?

(e) How does advertising differ from publicity?

(f) What is the role of middlemen in the distribution of consumer goods?

(g) What are the obligations of the banker towards its customers?

(h) What are the requirements that are expected from a good transport system?

SECTION B

Note: Attempt any three of the following:

Q2. Describe briefly the objectives of business. Do you agree with the statement, "Business is not mere money chasing but it should also aim at serving the community"? Justify your answer.

Q3. How do companies raise long term and medium term capital? Explain difference between equity shares and preference shares.

Q4. What are the factors that influence the choice of channel for distributing the goods? What do you mean by middlemen?

Q5. Describe different types of life insurance policies.

Q6. Why does the Government participate in business? Give main reasons. What is a public enterprise?

Q7. Describe the main features of public corporations. What are their main limitations?

ECO-1: BUSINESS ORGANISATION
June, 2011

Note: Attempt both Section-A and Section-B.

SECTION A

Q1. Attempt any four of the following:

(a) Distinguish between profession and employment.

Refer to June-2005, Q.No.-1

(b) Describe briefly different types of promoters of business.

Refer to Chapter-1, Q.No.-16

(c) Explain the differences between fixed capital and working capital.

Refer to December-2007, Q.No.-1(b)

(d) State the important points to be kept in mind while designing an advertisement message.

Refer to Chapter-3, Q.No.-4

(e) Outline the important steps necessary to be taken by a businessman before undertaking export- import business.

Refer to Chapter-3, Q.No.-16

(f) How is overdraft facility beneficial to the businessman?

Ans. Overdraft is a financial arrangement under which a current account holder is permitted by the bank to withdraw more than the credit balance in his account, upto an agreed limit. Thus, by nature, it is a temporary financial accommodation to be made use the customer occasionally. The overdraft facility is given to those who have a current account with the bank and whose business relations with the bank continue to be good,. Besides that, bank also considers the business of the customer, his reputation, how far the arrangement will help the customer to improve his business, and ability to repay the money to the bank.

An overdraft is granted either against collateral securities or against the personal security of the borrower. An overdraft arrangement is very advantageous to the borrower as interest is charged on the amount actually overdrawn by him. But it is not advantageous to the bank because, while he can charge interest on the amount actually overdrawn, he is required to keep at the disposal of the customer the full amount of overdraft sanctioned. In order to protect the interest of the banker agreement a minimum interest clause is included in the agreement, which required the customer to pay a minimum rate of interest on the sanctioned amount of overdraft, if the overdraft is not utilized fully. Bank should be very careful while granting overdraft facility to a customer, because in case of default by the customer to repay the overdraft, the bank has to go through long legal formalities. In order to be safe, the banks generally obtain a promissory note from the customer.

(g) Explain the difference between a public enterprise and a Private enterprise.
Refer to June-2008, Q.No.-7

(h) What is meant by a government company?
Refer to Chapter-5, Q.No.-8(3)

SECTION B

Note: Attempt any three of following:

Q2. Describe the facilities that are called 'Aid to Trade'. How is wholesale trade different from retail trade?
Refer to December-2009 Q.No.-8(b)

Q3. Explain the merits and limitations of the company form of business organization.
Refer to Chapter-1, Q.No.-10

Q4. "Speculative transactions are different from investment transaction". Elaborate.
Refer to June-2005, Q.No.-1(d)

Q5. State the services of retailers to consumers and explain the features of a super market.

Ans. Services of Retailers: As middlemen engaged in the distribution of goods, retailers deal with wholesalers and consumers. Manufacturers as well as wholesalers depend a great deal on retailers for reaching the ultimate consumers to supply various products. Retailers provide the necessary outlet for goods and thus render very useful service to the wholesalers and also to the producers indirectly. The services of retailers to the consumers are significant in several ways:

1. Holding ready stocks: By holding stocks, retailers supply varieties of goods of daily use to consumers. Besides, consumers are also given opportunity to make their choice from several varieties produced by different firms.

2. Display of goods: By displaying goods on shelves or in show-cases, retailers bring new products to the notice of customers. They also keep the customers informed about the latest varieties of goods available for sale by explaining their qualities and prices. Customers are also given demonstration of new products on the sales counter.

3. Advice to consumers: Very often retailers help the customers to make their decision to buy certain goods by advising them on the merits and use of particular varieties of products.

4. Personal services: A part from meeting the needs of different types of customers, retailers also offer a variety of services like home delivery, sale on credit, etc.

Now Refer to Page No.-79[Super Market]

Q6. How does foreign trade differ from the domestic trade? Can the change of the Government in particular country affect its foreign trade?

Ans. Differences between International Trade and Domestic Trade

Scope: Scope of international business is quite wide. It includes not only merchandise exports, but also trade in services, licensing and franchising as well as foreign investments. Domestic business pertains to a limited territory.

Though the firm has many business establishments in different locations all the trading activities are inside a single boundary.

Benefits: International business benefits both the nations and firms. Domestic business have lesser benefits when compared to the former.

• To the nations: Through international business nations gain by way of earning foreign exchange, more efficient use of domestic resources, greater prospects of growth and creation of employment opportunities. Domestic business as it is conducted locally there would be no much involvement of foreign currency. It can create employment opportunities too and the most important part is business since carried locally and always dealt with local resources the perfection in utilization of the same resources would obviously reap the benefits.

• To the firms: The advantages to the firms carrying business globally include prospects for higher profits, greater utilization of production capacities, way out to intense competition in domestic market and improved business vision. Profits in domestic trade are always lesser when compared to the profits of the firms dealing transactions globally.

Market Fluctuations: Firms conducting trade internationally can withstand these situations and huge losses as their operations are wide spread. Though they face losses in one area they may get profits in other areas, this provides for stabilizing during seasonal market fluctuations. Firms carrying business locally have to face this situation which results in low profits and in some cases losses too.

Modes of entry: A firm desirous of entering into international business has several options available to it. These range from exporting/importing to contract manufacturing abroad, licensing and franchising, joint ventures and setting up wholly owned subsidiaries abroad. Each entry mode has its own advantages and disadvantages which the firm needs to take into account while deciding as to which mode of entry it should prefer. Firms going for domestic trade does have the options but not too many as the former one. To establish business internationally firms initially have to complete many formalities which obviously is a tedious task. But to start a business locally the process is always an easy task. It doesn't require to process any difficult formalities.

Purvey: Providing goods and services as a business within a territory is much easier than doing the same globally. Restrictions such as custom procedures do not bother domestic entities but whereas globally operating firms need to follow complicated customs procedures and trade barriers like tariff etc.

Sharing of Technology: International business provides for sharing of the latest technology that is innovated in various firms across the globe which in consequence will improve the mode and quality of their production.

Political relations: International business obviously improve the political relations among the nations which gives rise to Cross-national cooperation and agreements. Nations co-operate more on transactional issues.

Q7. Describe briefly the various types of bank accounts that can be opened by a customer and explain the procedure for opening any one of these accounts.

Refer to Chapter-1, Q.No.-5, Page No.-98

Procedure for opening accounts

Opening of Fixed Deposit account:

For opening a fixed deposit account, the depositor as to fill in an application form available with the bank. The form contains particulars such as name of depositor, the amount of deposit, the period of deposit and the period of deposit and the specimen signature. The bank records the rate of interest payable and the due date of repayment. As cheques are not draws against a fixed deposit account, the banker need not ask for any introduction or reference as to the integrity and respectability of the depositor. After the deposit is received by the bank, an account is opened in the name of depositor in the ledger of the bank and the bank issues a fixed deposit receipt to the depositor. The receipt is an acknowledgement of the receipt of deposit by the bank. A deposit receipt is not a negotiable instrument and cannot be treated as a cheque.

Opening of a Current Account

Whenever any person or a group of persons or a firm wants to open a current account with a bank, they have to make a written request in the prescribed form. The forms contain the particulars about his name, his address, his trade or profession, his specimen signature and references etc. Before opening a current account in the name of a person, the bank should satisfy itself regarding the customer's character, integrity and respectability. For this purpose, the applicant must be introduced either by a respectable person knows to the bank or knows to the staff of the branch. If an account is opened without proper introduction, cases of fraud or misrepresentation may occur and the bank and the general public may suffer losses. After all the above formalities are over, the bank could receive the initial or first deposit from the customer. When an account is opened, the bank supplies to the customer a 'Pay-in slips book', a cheque book and a pass book. Now in place of the pass book, the banks send to their customers every month a statement of account showing therein the transactions that have taken place during the month.

Opening a Savings Bank Account

The procedure of opening a savings bank account is similar to the procedure of opening a current account. For opening a savings bank account, the customer has to fill up the prescribed form, giving details about his name, address, occupation, etc. Before opening the account, the bank should seek proper introduction to satisfy himself about the integrity and respectability of the applicant. The bank should obtain specimen signature of the applicant. This account can be opened by depositing a minimum balance prescribed by the bank. The bank then opens an account in his ledger and provides the customer with a pay-in slip book, a cheque book (if customer wants) and a Pass Book.

ECO-1: BUSINESS ORGANISATION
December, 2011

Note: Attempt both Part A and Part B.

PART A

Q1. Distinguish between any two of the following:
(a) Business and commerce
(b) Equity shares and preference share
(c) Indoor advertising and outdoor advertising
(d) Bonded warehouse and public warehouse

Q2. Write short notes on any two of the following:
(a) Clearing and forwarding agents
(b) Pricing Policy of Public utilities
(c) Doctrine of subrogation
(d) Functional middlemen

PART B

Attempt any three of the following questions:
Q3. Explain the factors that determine the choice of the form of business organisation.

Q4. What is capital structure? Discuss various factors to be kept in mind while deciding capital structure of the company.

Q5. "There is no need for the presence of wholesalers in the distribution channel and they should be eliminated." Discuss.

Q6. "All business risks are not insurable." In the light of this statement, explain insurable risks and non-insurable risks.

Q7. (a) Differentiate between a Government company and a public limited company.
(b) What are the problems of public enterprises?

Q8. State the documents that must accompany an export shipment. Describe them briefly.

ECO-1: BUSINESS ORGANISATION
June, 2012

Note: Attempt both Part-A and Part-B.

PART A

Q1. Distinguish between any two of the following:

(a) Sole trader and partnership

Ans. Sole trader

J.L. Hanson defines sole trader as "a type of business unit where one person is solely responsible for providing the capital for bearing the risk of the enterprise and for the management of the business".

The sole trader organization (also called proprietorship) is the oldest form of organization and the most common form of organization for small business even today. It is the simplest and easiest to form. What is required is that an individual decides about the type of business to be started and arranges the necessary capital. Required capital may be mobilized from his own saving, or may be borrowed from friends and relatives. The business may be carried either in a portion of his own residence or in a rented building. The person generally manages the business on his own. He may also take the help of his family members or employ some persons, if necessary. He can take advice from others in running the business, but his own will be the final decision. Thus, the sole trader enjoys full control over the affairs of the firm. He enjoys all the profits earned by the business. So in case of loss, naturally, he has to bear the full brunt of it.

Thus, we can now define sole trader organization as "one man's business in which an individual produces independently with his own capital, skill and intelligence and is entitled to receive all the profits and assumes all the risks of ownership".

Partnership

As Defined by J.L. Hanson, "a partnership is a form of business organization in which two or more persons upto a maximum of twenty join together to undertake some form of business activity".

The Indian Partnership Act, 1932 defined partnership as "the relation between persons who have agreed to share the profits of business carried on by all or any of them acting for all".

The Uniform Partnership Act of the USA defines partnership "as an association of two or more persons to carry on as co-owners of a business for profit".

Based on the above definitions, we can state that partnership is an association of two or more persons who have joined together to share the profits of business carried on by all or any of them acting for all.

(b) Capital market and money market

Ans. Capital market actually denotes the arrangements whereby transactions of money capital (not capital goods) are facilitated. In other words, transactions involving procurement of funds and supply of funds which take place among individuals and various organizations may be regarded as the capital market. The capital market is not located in a particular place. Nor there are fixed categories of investors and dealers in the capital market.

Money market refers to transactions involving borrowing and lending of money for short periods for which again there is no definite place set aside in a town. Thus, we can say that money market is the market for short-term funds.

(c) Direct channels and indirect channels of distribution

Ans. Direct channels: When the producers sell their goods directly to the consumers it is called a direct channel. No middlemen is present between the producer and the consumer.

They establish direct link with the consumers through travelling salesmen or through their own retail shops or show-rooms. The producer or manufacturer may employ salesmen to book orders by contacting the potential users, and supply may be arranged from the stock held by the producer himself. Alternatively, the producer may set up retail shops/show rooms in different localities and sell goods directly to the customers as shown below.

(1) Producer → Travelling Salesman → Consumer

(2) Producer → Retail shop/showroom → Consumer

Indirect channels: In the case of all the products, it is not possible for the manufacturer to supply goods directly to the consumers. So middlemen like wholesaler, retailer and mercantile agents may be engaged in the channel of distribution. When the middlemen are engaged, it is called an indirect channel. As shown below, there could be four indirect channels.

(1) Producer → Retailer → Consumer

(2) Producer → Wholesaler → Consumer

(3) Producer → Wholesaler → Retailer → Consumer

(4) Producer → Agent → Wholesaler → Retailer → Consumer

(d) Current account and savings bank account

Ans. Current Account

A current account is a running and active account which may be operated upon any number of times during a working day. In current account, amount can be deposited and withdrawn at any time without giving any notice. Since the amount from this account is repayable on demand, the banks are required to keep sufficient cash to meet such demands. Current accounts are intended for businessmen, joint stock companies, public institutions, etc., whose banking transactions happen to be numerous on every working day. The banks charge incidental charges on an unremunerative current account for the work and expenses involved in its maintenance.

The main advantage of current account is that the customers are relieved from the botheration of handling cash. Third party cheques with endorsements can be deposited in the current account for collection and credit to customer's account. Overdraft facilities are given in this type of account and loans and advances are granted by the bank.

Savings Account

A savings bank account is opened and operated by people who wish to save a part of their income for their future needs and also earn some interest on their deposits. This type of account is intended to promote the habit of saving among depositors, therefore, some restrictions have been imposed on the number and the amount of withdrawals from this account. The banks allow interest on the minimum balance standing to the credit of an account during the period from the 10th day of the month to the last day of every month.

A customer operates this account through these documents - a pay-in slip (for depositing money in the account), a cheque or withdrawal form (for withdrawing or payment to others) and a pass book.

Q2. Write short notes on any two of the following:

(a) Containerization

Refer to June-2003, Q.No.-4(d)

(b) Public utility undertaking

Refer to Chapter-5, Q.No.-9

(c) Fire insurance

Refer to Chapter-4, Q.No.-12(iii)

(d) Chain stores

Ans. Chain stores are retail outlets that share a brand and central management, and usually have standardized business methods and practices. The United States Bureau of the Census of the United States Department of Commerce defines a chain as a group of reasonably similar stores in the same kind or field of business, under one ownership and management, merchandised wholly or largely from one or more central points. However, there is a disagreement among authorities as to the minimum number of stores forming a chain system. Although the Bureau of the Census for convenience sets four as the minimum number of stores which may constitute a chain, others feel that any group of two or more stores may be organized as a chain. The Federal Trade Commission defines a chain as an organization "owning a controlling interest in two or more establishments which sell substantially similar merchandise at retail." Thus, two stores are said to constitute a chain and emphasis is not placed on centralized management.

PART B

Attempt *any three* of the following questions:

Q3. What is a joint stock company? Explain as to how it overcomes the limitations of partnership form of organization.

Ans. A **joint-stock company** is a business entity which is owned by shareholders. Each shareholder owns the portion of the company in proportion to his or her ownership of the company's shares. In other words, a company form of business organization is known as a Joint Stock Company. It is a voluntary association of persons who generally contribute capital to carry on a particular type of business, which is established by law and can be dissolved only by law. Persons who contribute capital become members of the company. This form of business has a legal existence separate from its members, which means even if its members die, the company remains in existence. This form of business organizations generally requires huge capital investment, which is contributed by its members. The total capital of a joint stock company is called share capital and it is divided into a number of units called shares. Thus, every member has some shares in the business depending upon the amount of capital contributed by him. Hence, members are also called shareholders.

A partnership firm must have more than one person involved in the business. But legally speaking, a partnership firm has no existence apart from its partners. On the other hand, a company after it is formed acquires a separate legal identity. It is regarded in law as a separate entity distinct from the members who join it.

Ownership of stock confers a large number of privileges. The company is managed on behalf of the shareholders by a Board of Directors, elected at an Annual General Meeting. The shareholders also vote to accept or reject an Annual Report and audited set of accounts. The shareholders are usually liable for any of the company debts that exceed the company's ability to pay. However, the limit of their liability only extends to the face value of their shareholding. This concept of limited liability largely accounts for the success of this form of business organization. It also entitles the owners to a share in the company's net profit.

In a partnership firm, the number of partners cannot exceed 20. Therefore, there is a limit to the contribution of capital. Secondly, even if the partners could contribute a large amount of capital, they would hesitate to do so considering the risk involved in business and their unlimited liability. Mainly to take care of these two problems, a company form of business organization came into existence.

Due to the availability of large financial resources and technical expertise, it is possible for the companies to have large-scale production. It enables the company to produce more efficiently and at lower cost.

Q4. "Stock exchange is a barometer of the economic and business conditions in a country". Discuss.

Ans. Stock exchange is a barometer which indicates the general conditions and the atmosphere of business.

The trend of values on the market reveals the trend in economic conditions, economic prospects and industrial prospects within the economy. The industrialist, the investor and the student of economics and even the politicians can feel the pulse of the nation by watching and studying the trends of prices on the stock exchange.

It provides much needed mobility of capital and directs the flow of capital into profitable and more successful industrial enterprises and retards its flow into enterprises with less justification for development. Thus, it brings about a fine balance between demand and supply of capital.

A developing country can by proper adjustment make a good deal of use of this weapon to faster justifiable industries. In other words, it equates the flow of savings to economic needs.

A stock exchange helps in the process of economic development of the country. The rapid increase in the growth of corporate sector in the recent decades has been possible partly because of the facilities provided by the stock exchange. A stock exchange serves as an agency of capital formation. By providing liquidity and price continuity to securities, it induces the public to save and invest in corporate enterprises. As a ready and continuous market for securities, the stock exchange facilitates shifting of investments to more productive channels. Investors divert their funds into those securities which are safer and give higher yields. Thus, the stock exchange helps in better utilization of the country's financial resources. It is the citadel of the capital market.

A stock exchange is a very sensitive barometer of business conditions in the society. Booms, depressions and other important events affect prices of securities. Price trends on the stock exchange reflect the economic climate in the country. Stock exchanges are not merely chief theatres of business transactions/activities, they are also barometers which indicate the general business conditions in the society.

Now, Refer to Page-50 [Barometer of economic and business conditions]

Q5. Why are the channels of distribution different for different products?

Refer to June-2010, Q.No.-5

Q6. "Banks provide various types of advances to its customers according to their needs and repayment capacity" Explain.

Ans. Different types of advances provided by banks to its customers are:

(1) Loans

A loan is a financial arrangement under which an advance is granted by the bank to the borrower on a separate account called the loan account. When a loan is granted against security or otherwise, the entire amount of loan is paid to the borrower in lump sum either in cash or by transferring the amount to his account in the bank. Whenever borrower repays some money, the loan account is credited by that amount and the loan account is debited with the account of interest and incidental charges. Interest is charged on the whole amount of loan sanctioned, irrespective of the amount actually withdrawn by the borrower. However, the rate of interest on loan is slightly lower than that charged in an overdraft and a cash credit.

The loans to individuals are granted on the basis of personal security and guarantee by another person. Loans to trade, industry or agriculture are granted against tangible and intangible securities. **A secured loan or advances** means a loan or an advance made on the security of assets, the market value of which is not at any time less than the amount of such loan or advance.

The banks prefer to grant loans because of the following three reasons: (i) the bank can collect interest on the entire amount of loan sanctioned, (ii) it involves very little accounting work, (iii) the bank can review the loan account periodically. The main drawback of the loan system is that every time a loan is needed, it is to be negotiated afresh. Further, the banks have no control over the use of funds borrowed by the customer.

Now, Refer to June-2011, Q.No.-1(f)

(2) Cash Credit

Case credit is the main method of lending by banks in India. Cash Credit is a financial arrangement between the bank and the customer under which a bank allows his customer to borrow money upto a certain limit against the security of tangible assets or guarantees. The amount is credited to a separate account and the customer is allowed to operate the account.

In the case of cash credit, the borrower need not withdraw the whole amount at once. He can withdraw the amount in installments as and when needed. Further, he can deposit into the account any surplus amount which he has in his hands. Thus, it is an active running account to which deposits and withdrawals may be effected frequently. However, the debit balance in a cash credit account on any day should not exceed the cash credit limit. A cash credit is usually a more permanent financial arrangement than an overdraft.

In the case of cash credit, interest is charged not on the amount of cash credit sanctioned to him, but on the amount actually utilized by him for the actual of utilization.

(3) Discounting of Bills

Discounting of bills of exchange is another form of leading. Under this system the bank takes a bill of exchange maturing within a short time, say 60 days or 90 days and credits the customer's account with the amount of the bill after some discount. The bank waits upto the date of maturity of the bill and presents it on the date of maturity to the drawee for payment. Since the bank has to wait till the date of maturity, the banks charge interest for the remaining duration of the bill and this amount is known as ‘discount’. For example, a bill of Rs. 5,000 payable after 3 months is discounted @ 6 per cent, the bank will credit the customer’s account with Rs. 4,925 only.

Banks normally accept only such bills which are considered eligible for discount under the directions of Reserve Bank of India. The bills mostly discounted are documentary bills i.e., a bill of exchange accompanied by documents of title to goods. In case the bill is dishonoured on the due date, the bank recovers the amount of the bill together with interest and other charges from the customer. The bank has to take care that the dishonoured bills are immediately sent to the customer to enable him to take the necessary legal action.

The main advantage of discounting of bills is that, though the bank has no tangible assets with it as security, the bank can recover the full amount of the bill from the customer by debiting his account. It is a method of short-term financing. The bank is certain the after the stated period, the amount will be realized, so the bank can utilize its funds more profitably.

Q7. In the present day context, do you think it is necessary for the government to directly participate in business? State your views.

Refer to Chapter-5, Q.No.-3

Q8. Explain the procedure, one has to follow when goods are imported.

Refer to Chapter-3, Q.No.-16

ECO-1: BUSINESS ORGANISATION
December, 2012

Note: Attempt both Part-A and Part-B

PART A

Q1. Distinguish between any two of the following:
(a) Entrepreneur and promoter.
(b) Ownership capital and borrowed capital.
(c) Intensive distribution and exclusive distribution.
(d) Time deposits and demand deposits.

Q2. Write short notes on any two of the following:
(a) Partnership deed.
(b) Factoring.
(c) Speculation and gambling.
(d) Hire purchase trading.

PART B

Attempt any three of the following questions:
Q3. "Company form of organisation is most suitable in the modern times". Do you agree with this view? Explain.
Q4. What do you mean by capital structure? Explain the factors determining the capital structure of a manufacturing company.
Q5. What is a stock exchange? Explain its main functions.
Q6. Explain the merits and demerits of various advertising media.
Q7. "Foreign trade is an engine of economic growth in a country". Comment on this statement in Indian context.
Q8. Sate the essential characteristics of public utility undertakings. Highlight the problems faced by them.

ECO-1: BUSINESS ORGANISATION
June, 2013

Note: Attempt both Part-A and Part-B.

PART A

Q1. Distinguish between any two of the following:
(a) Employment and Profession
(b) Private limited company and Public limited company
(c) Bank overdraft and Cash credit
(d) Joint life policy and Group insurance

Q2. Write short notes on any two of the following:
(a) Hypothecation
(b) Leasing
(c) Public utility undertaking
(d) Underwriting

PART B

Attempt any three of the following questions:
Q3. Discuss the role of entrepreneur in business promotion. Outline the basic characteristics of an entrepreneur.

Q4. State the various methods of raising long term funds for a business organisation and explain the merits and demerits of any one of these methods.

Q5. "Advertisement is a waste". Comment on this statement.

Q6. Discuss the factors influencing the choice of channels of distribution.

Q7. Define business risk. What are the various types of business risks? How do you manage them?

Q8. (a) Explain the characteristics of a government company.
(b) Why is government's direct participation in business considered necessary?

ECO-1: BUSINESS ORGANISATION
December, 2013

Note: Attempt both Section-A and Section-B.

SECTION A

Q1. Attempt any four of the following:
(a) Distinguish between economic and non-economic activities.
(b) Explain entrepreneurship and its main characteristics.
(c) What do you mean by public deposits? State the conditions to be satisfied if a small scale unit wants to exceed the limits.
(d) What is meant by margin trading? Explain with an example.
(e) Explain publicity and its different forms.
(f) State the services of wholesalers to the retailers.
(g) What do you mean by mortgage? Explain its importance in business.
(h) Enumerate the salient features of the public enterprises.

SECTION B

Attempt any three of the following questions:
Q2. What is meant by trade? Describe briefly different aids to trade.

Q3. Explain the cooperative form of business organisation and state its merits and limitations.

Q4. Describe the methods of raising long-term capital for a company.

Q5. What is the importance of channel of distribution in business? Briefly explain the channels of distribution used for consumer goods.

Q6. How does foreign trade help economic development of a country? State its inherent problems.

Q7. Describe the various steps involved in risk management in business.

ECO-1: BUSINESS ORGANISATION
June, 2014

Note: Attempt both Section-A and Section-B.

SECTION A

Q1. Attempt any four of the following:

(a) Distinguish between private limited company and public limited company.

(b) Write a short note on bank overdraft.

(c) How is Industrial Finance corporation of India helpful in the industrial development?

(d) Explain the concept of speculation at stock exchanges.

(e) State with reasons of your choice of media of advertising for a low priced detergent in the rural areas.

(f) Describe briefly the importance of transport in trade.

(g) Enumerate the major reasons for the government participation in business.

(h) Distinguish between current bank account and savings bank accounts.

SECTION B

Note: Attempt any three of the following:

Q2. What do you mean by partnership? Enumerate the main features of partnership form of business organisation.

Q3. Define capital structure. Describe the factors that determine the capital structure of a company.

Q4. Discuss the primary and secondary functions of a stock exchange.

Q5. How does advertisement help the business? Also state its adverse effects.

Q6. Outline the relationship between a banker and its customer. What are the obligations of a bank towards them?

Q7. Describe the distinctive features of public utilities.

ECO-1: BUSINESS ORGANISATION
December, 2014

Note: Attempt both Part-A and Part-B.

PART A

Q1. Distinguish between any two of the following:
(a) Wholesale trade and retail trade
(b) Entrepreneur and promoter
(c) Statutory company and registered company
(d) Publicity and advertisement

Q2. Write short notes on any two of the following:
(a) Bank overdraft
(b) Margin trading
(c) Outdoor media
(d) Bill of lading

PART B

Attempt any three of the following questions:
Q3. What do you mean by business? Describe salient features of business and discuss its economic objectives.

Q4. (a) Describe the functions of Industrial Development Bank of India (IDBI).
(b) How is it different from Industrial Finance Corporation of India (IFCI)?

Q5. What do you mean by foreign trade? Discuss the importance of foreign trade. Explain the common problems faced in foreign trade.

Q6. What do you mean by risk management? Explain the various steps followed in risk management.

Q7. "Efficient transportation is an integral part of economic growth". Elaborate.

Q8. What is meant by departmental form of organisation? Discuss its merits and demerits.

ECO-1: BUSINESS ORGANISATION
June, 2015

Note: Attempt both Part-A and Part-B.

PART A

Q1. Distinguish between any two of the following:
(a) Fixed capital and working capital
(b) Direct and indirect distribution channel
(c) Departmental store and supermarket
(d) Pledge and hypothecation

Q2. Write short notes on any two of the following:
(a) Aids to trade
(b) International financial institutions
(c) Outdoor media
(d) Insurable risk

PART B

Attempt any three of the following questions:
Q3. What do you mean by a company? Explain its salient features.

Q4. Outline the characteristics of stock exchange. Describe its primary and secondary functions.

Q5. Define advertising and discuss types of media and their characteristics.

Q6. "Retailer is an important link in the supply chain of consumer goods." Elaborate by giving suitable examples.

Q7. What is meant by insurance? Explain briefly various types of insurances.

Q8. What is meant by public utilities? Describe the distinctive features of public utilities.

ECO-1: BUSINESS ORGANISATION
December, 2015

Note: Attempt both Part-A and Part-B.

PART A

Q1. Attempt any four of the following:

(a) Distinguish between non-economic and economic activities of human beings.
(b) State the qualities of a good entrepreneur.
(c) Describe the methods of raising long-term capital.
(d) State briefly the rules for listing of securities on a stock exchange.
(e) Distinguish between advertisement and publicity.
(f) State channels of distribution of industrial goods.

PART B

Attempt any three of the following questions:

Q2. What is meant by cooperative form of organisation? Enumerate its main features.

Q3. What is meant by long-term finance? Describe various sources of long-term finance.

Q4. How does speculation differ from gambling? State the various factors affecting prices of securities in a stock exchange.

Q5. Explain the difference between functional and merchant middlemen. How do they help the business activities?

Q6. How do commercial banks contribute to the economic development of a country? Explain.

Q7. State the merits and demerits of government participation in business.

ECO-1: BUSINESS ORGANISATION
June, 2016

Note: Attempt both Part-A and Part-B.

PART A

Q1. Attempt any four of the following:
(a) Distinguish between entrepreneur and promoter.
(b) State the characteristics of a capital market.
(c) Explain forward delivery contracts at the stock exchange.
(d) State the various outdoor media of advertising.
(e) Enumerate essentials of a good transport system.
(f) How does a public enterprise differ from private enterprise? Explain.

PART B

Attempt any three of the following:
Q2. Name the four forms of business organisation. Describe briefly the requisites of an ideal form of business organisation.

Q3. What is a stock exchange? Describe briefly its various functions.

Q4. Suppose your company has launched a detergent of low price. As the chief of the marketing wing, how will you choose an appropriate media for making it popular?

Q5. State the importance of distribution channel in the promotion of business. Describe briefly the factors that influence the choice of the channel.

Q6. Suppose your company decides to set up a manufacturing unit of apparels. How will you proceed for importing the necessary machinery and technology for the same? Explain.

Q7. What do you mean by risk management? Describe briefly the insurable risks and the non-insurable risks.

Note: Attempt any five questions. All question carry equal marks.

Q1. Define the term 'business' and state its essential features. How is it different from profession?
Ans. Refer to Chapter-1, Q.No.-1 and Q.No.-2

Q2. What do you mean by cooperative form of organisation? Explain its merits and demerits.
Ans. Refer to Chapter-1, Q.No.-11

Q3. What are the various methods of raising short-term capital? Explain them briefly.
Ans. Refer to Chapter-2, Q.No.-4 and Dec-2004, Q.No.-1(b)

Factoring: The amounts due to a company from customers on account of credit sale generally remain outstanding during the period of credit allowed i.e. till the dues are collected from the debtors. If necessary, book debts may be assigned to a bank and cash realised in advance from the bank. By this arrangement the responsibility of collecting the debtors' balances is taken over by the bank on payment of specified charges by the company. This is a method of raising short-term capital and known as 'factoring'. It helps companies to secure finance against debtor's balances before the debts are due for realisation, and incidentally also helps in saving the effort of collecting the book debts. The bank charges payable for the purpose is treated as the cost of raising funds. Keeping in view the risk of bad debts, the amount to be made available by banks is calculated so as to provide for a margin for non-realisation of debts. The disadvantage of factoring is that customers who are in genuine difficulty do not get the facility of delaying payment which they might have otherwise got from the company.
Bank Overdraft and Cash Credit: Arranging cash credit and overdraft with commercial banks is a common method adopted by companies for meeting short-term financial requirements. Cash credit refers to an arrangement on a continuing basis whereby the commercial bank allows money to be drawn as advance from time to time within a specified limit known as cash credit limit. This facility is granted against the security of goods in stock, or promissory notes bearing a second signature, or other marketable instruments like Government bonds. The company is allowed to draw whatever amount is

required at different times within the limit agreed upon. The cash credit limit may be revised according to the value of securities. The money drawn can be repaid as and when possible. Interest is charged on the actual amount withdrawn.

Overdraft is a temporary arrangement with the bank which permits the company overdraw from its current deposit account with the bank upto a certain limit. The overdraft facility is also granted against securities as in the case of cash credit. Interest is charged only on the amount actually overdrawn. The rate of interest charged on cash credit and overdraft is relatively much higher than the rate of interest on bank deposits. But this method of financing has the flexibility of allowing funds to be drawn for short-term purposes according to changing needs which depend on business conditions.

Public Deposits: Companies often find it convenient and necessary to raise funds by inviting their shareholders, employees and the general public to deposit their savings with the company. The Companies Act permits such deposits to be received for a period up to 3 years at a time. Thus, public deposits can be raised by companies to meet their short-term and medium-term financial needs. It is a simple methods of raising finance for which the company has only to advertise in the newspapers giving particulars about its financial position as prescribed by the Companies Act. The deposits are not required to be covered by mortgaging assets or by other securities. Moreover deposits can be invited by offering a higher rate of interest than the interest on bank deposits.

But companies are not permitted to raise unlimited amounts of fund through public deposits. The aggregate of all outstanding deposits cannot exceed 25% of the paid up capital and free reserves of the company. Interest to be allowed on deposits must also be in accordance with the rate fixed by the Government. Further, it is laid down in the Companies Act that at the beginning of each year, the company must deposit in a bank at least 10% of the deposits maturing during that year, or invest an equivalent amount in Government securities for repayment of deposits. Besides, the company has to file a return or statement every year with the Registrar of Companies giving all information relating to the deposits.

However, small scale industries (i.e. manufacturing companies with investment in plant and machinery not exceeding Rs. 35 lakhs) are exempted from the restrictions as to the maximum limit of deposits if the following conditions are satisfied.

(i) The amount of deposit does not exceed Rs. 8 lakhs or the amount of paid up capital whichever is less.

(ii) The paid up capital does not exceed Rs. 12 lakhs.

(iii) The number of depositors is not more than 50%.

(iv) There is no invitation to the public for deposits.

Q4. Discuss the various functions performed by wholesalers.
Ans. Refer to Chapter-3, Q.No.-10

Q5. Distinguish between any two of the following:
(a) Loan and Overdraft
Ans. Refer to Chapter-4, Q.No.-6

(b) Cash Credit and Overdraft
Ans. Refer to Chapter-4, Q.No.-6

(c) Pledge and Hypothecation
Ans. Refer to Chapter-4, Q.No.-8

Q6. Explain the features of a fire policy and state the various types of fire policies issued by insurance companies.
Ans. Refer to Chapter-4, Q.No.-12

Types of Fire Policies: Broadly, there are six types of fire insurance policies, as explained below:
• Specific Policy where the liability of the insurer is limited to a specified amount, which is normally less than the actual value of the property insured.
• Valued Policy where the insurer agrees to pay a fixed amount in the event of loss, irrespective of the actual loss suffered. Under this policy, the insured recovers a fixed amount, irrespective of the amount of actual damage.
• Floating Policy where the amount of the policy may vary from time to time. This type of policy is useful in the case of goods in store where quantity and value change from time to time.
• Replacement Policy where the insurer has the option to replace the property/ goods damaged by fire, instead of paying the loss by cash.
• Loss of Profit Policy where insured is protected against the loss of profit due to dislocation of business due to fire. Under this policy, insurer compensates to the extent of the loss in profits.
• Comprehensive Policy which provides cover against not only fire but also several other risks such as lightning, riot, earthquake, food, storm, burglary, war, etc.

Q7. What is a public enterprise? State the features and objectives of a public enterprise.
Ans. Refer to Chapter-5, Q.No.-4

Q8. Write short notes on any two of the following:

(a) Departmental Store

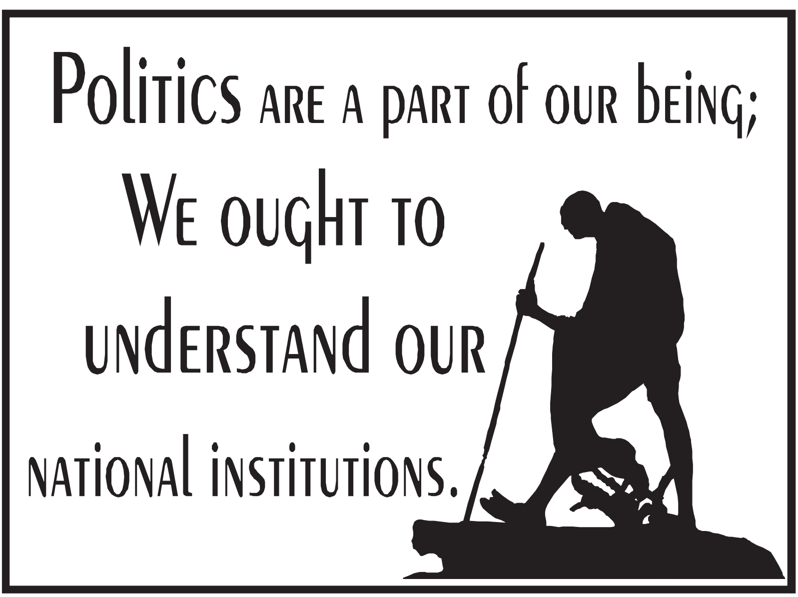
Ans. Refer to Chapter-3, Q.No.-13(1)

(b) Public Corporation

Ans. Refer to Chapter-5, Q.No.-8(2)

(c) Pricing policy followed by public utilities

Ans. Refer to Chapter-5, Q.No.-11



ECO-1: BUSINESS ORGANISATION
June, 2017

Note: Attempt any five questions. All questions carry equal marks.

Q1. Explain the features of an ideal form of business organisation, and state factors affecting the choice of form of business organisation.
Ans. Refer to Chapter-1, Q.No.-12

Q2. Discuss the role of an entrepreneur in business promotion. How does an entrepreneur differ from a promoter?
Ans. Refer to Chapter-1, Q.No.-15
Sometimes a distinction is made between 'entrepreneurs' and 'promoters' of business. Those who are innovators and risk-bearers are strictly known as 'entrepreneurs' while those who take steps to set up the business and make it operational are known as 'promoters'. In actual practice, however, this distinction does not hold good. Entrepreneurship (act of entrepreneurs) does not remain confined only to recognition of business opportunities and preparedness to do something new. It does not end with the entrepreneur undertaking to bear the risks of business. It includes planning for the business and taking necessary steps to put it into operation. After all, a business becomes a business only when it gets going. Thus, in a wider sense we cannot make a difference between the role of an entrepreneur and the role of promoter.

Q3. What is a Stock Exchange? Describe the functions of a Stock Exchange.
Ans. Refer to Chapter-2, Q.No.-10

Q4. State the main purpose of advertising and suggest the guidelines for designing an effective advertisement.
Ans. Refer to Dec.-2006, Q.No.-5

Q5. Discuss the various problems faced by an organisation in managing foreign trade.
Ans. Refer to Chapter-3, Q.No.-15

Q6. Distinguish between any two of the following:
(a) Voyage policy and Time Policy
Ans. Voyage Policies: This type of policy covers a ship or cargo during a specified voyage only. Thus, the limits of the risk are from the port of departure

to the port of destination. The risk which is covered starts from the departure of ship from the port and it ends when that ship reaches the port of destination. For example, we are shipping the export cargo from Bombay to Amsterdam in Netherlands and we have taken a voyage policy. This policy covers the risk of damage to cargo from Bombay port till it reaches the Amsterdam port. In the case of a voyage policy, issuer is not liable if the destination of the ship is changed or the ship deviates from the agreed route. However, deviation from the agreed route is allowed when it is necessary for the safety of ship/cargo or saving the human life or any other circumstance stated in the contract.
Time Policy: This type of policy covers the risk during a stated period of time irrespective of number of voyages made. This policy would cover all the risks from the perils of sea for a stated period of time, say 1st April 1998 to 30th March 1999. Normally a time policy covers a period not more than 12 months. However, most time policies include a *continuation clause* providing against expiration of the policy if the ship is still on the voyage. A monthly prorata premium is payable for the continuation.

(b) Risk avoidance and Loss prevention
Ans. Refer to Chapter-4, Q.No.-10

(c) Life insurance and Fire insurance
Ans. Refer to Chapter-4, Q.No.-12 (1) and (3)

Q7. Explain the factors taken into account while selecting a proper mode of transport for despatch of goods.
Ans. Refer to Chapter-4, Q.No.-16

Q8. Write short notes on any two of the following:
(a) Government Company
Ans. Refer to Chapter-5, Q.No.-7(iii)

(b) Sales policy of Public Utilities
Ans. Sales policies of public utilities are given below:
(1) The products or services offered by public utilities are 'essential' requirements of the public and have usually large demand from the public.
(2) The public utilities do not generally have rivals or competitors. A particular product is supplied by one undertaking in a particular area. So there is no possibility of different rates being charged by different producers in the same area. So there is no necessity for price discount.
(3) These undertakings are granted franchise by the government. They had the right to interfere with private property as well as right to use public property (roads, land, buildings, etc.).

(4) There are no middlemen or intermediaries for sale of their products or services. They sell directly to their consumers or sell through their own distribution network. For example water supply, electric supply, and transport undertakings come in direct contract with the consumers. Therefore, they have to offer best possible terms to users of these services.

(5) Unlike other commercial concerns, public utility undertakings do not have the problems of credit collection from the customers. In some cases, as in electricity undertakings, the supply is stopped if there is default in payment of bills by a specified date. In some cases, the dealings are on cash basis, as in railways and road transport undertakings.

(6) There is no necessity for the public utility undertakings to advertise their goods and services like other business units. However, they have to inform the public about the service which they provide. For example, a transport undertaking has to keep the public informed about the new services introduced from time to time on different routes, changes in the routes, changes in the timings, etc. Such information facilitates the customers in utilising the service which ultimately leads to utilisation of full capacity.

(c) Public Enterprise

Ans. Refer to Dec.-2004, Q.No.-1(g)

Whenever you do a thing, act as if all the world watching.

- Thomas Jefferson

ECO-1: BUSINESS ORGANISATION
December, 2017

Note: Attempt both Part-A and Part-B.

PART - A

Q1. Attempt any four of the following:
(a) Briefly explain the advantages of raising funds through the issue of debentures.
(b) Differentiate between business and profession.
(c) Explain the concept of 'entrepreneurship'.
(d) Write a short note on 'Recurring Deposit Account'.
(e) What are the essentials of a good transport system?
(f) State the objectives of Public Enterprises.

PART - B

Attempt any three of the following questions:
Q2. What do you mean by 'business risk'? Explain the process of risk management.

Q3. What is meant by Public Utility Undertaking? Discuss the broad aspects of their pricing policies.

Q4. What is a stock exchange? Explain the factors affecting the prices at a stock exchange.

Q5. Briefly describe the role of an entrepreneur in business promotion. How does an entrepreneur differ from a promoter?

Q6. Explain the significance of foreign trade for a country, and state the problems encountered in foreign trade by Indian entrepreneurs.

ECO-1: BUSINESS ORGANISATION
June, 2018

Note: Attempt both Part-A and Part-B.

PART-A

Q1. Attempt any four of the following:

(a) Write a short note on 'underwriting'.

Ans. Refer to Chapter-2, Q.No.-9 (Pg. No.-48)

(b) Differentiate between Advertisement and Publicity.

Ans. Refer to Chapter-3, Q.No.-1 (Pg. No.-63)

(c) State the services rendered by the retailers to the consumers.

Ans. Refer to Chapter-3, Q.No.-11 (Pg. No.-75)

(d) Briefly explain the merits of Partnership form of organisation.

Ans. Refer to Chapter-1, Q.No.-7 (Pg. No.-9)

(e) Briefly explain the procedure of raising funds through public deposits.

Ans. Refer to Chapter-2, Q.No.-6 (Pg. No.-41)

(f) State the problems of Public Enterprises.

Ans. Refer to Chapter-5, Q.No.-6 (Pg. No.-140)

PART - B

Attempt any three of the following questions:

Q2. Define 'Advertising Media'. State its different types and the requisites of an ideal medium.

Ans. Advertising media refers to the various media channels through which advertising is done. Advertising media is used for showcasing promotional content which communicated in various forms such as text, speech, images, videos using TV, radio, online, outdoor etc. Basically they are channels through which companies can advertise their products and services to reach to customers.

Types of advertising media

Advertising media is an important domain in business and advertising. With the passage of time, there have been several ways in which ads are being showcased and can be communicated to customers. There are different types of advertising media present. Depending upon various parameters like budget, reach, customer preferences etc companies can choose the required advertising media and help boost their brand. Some of the most important types of advertising media are:

(1) Broadest media: TV and radio are two of the most important advertising media known as broadcast media.

Television: Televisions have become a very important tool to advertise for companies. Companies can targets serials, reality shows, sports events, live events etc which are showcased on TV's and understand the demographics of the people watching the TV. TV channels are anyways classified as news, sports, knowledge, entertainment, movies, kids etc. This helps advertisers to pick and choose the channel. Thus TV is one of the most widely used advertising media in the world. Advertising slots are sold by broadcasting companies and channels based in popularity of TV shows, TRPs etc.

Radio: As a tool for marketing and advertising, radio is the most cost effective tool which a customer can have. Since radios have are high penetration and are easy for customers to buy, they are a good tool for advertising. Radios enable companies to reach out to a wide range of customers. Since radio cater to the needs of a particular city or region, it is a good ways to advertise based on customers selected from geographic segmentation. Thus, radio is one of the most effective tools as advertising media.

(2) Print Media: Advertising media like newspapers, magazines, leaflets, brochures, billboards, signages, direct mail and other print publications come under print media. With the massive reach of print media, it became a popular tool for advertising. Print media caters to a regional audience and is published in different languages. Hence, print media cater to a niche audience as compared to broadcast advertising media tools like TV or radio.

(3) Online Media: With the consistent growth in internet penetration, companies have started using online media for promotion through advertising. People are connected to the internet through social media, website browsing etc. This gives an opportunity to companies to use this advertising media and cater to customers using Online ads, blogs, content advertising, affiliate marketing etc are all done using online as an advertising media.

(4) Outdoor Media: Another popular form of advertising is using outdoor hoardings, billboards, OOH (out of home) media etc. it basically useful in capturing those customers who are travelling from one place to another. This gives an opportunity to companies to use outdoor advertising media to create brand awareness by putting large bill boards and hoardings above buildings, near streets etc to give maximum visibility.

(5) Mobile: With the increasing penetration and usage of mobile phones, mobile advertising has become a critical aspect for every business. Mobile as an advertising media helps to reach out to customer by promoting messages through SMS, social media chat groups etc. Online and mobile media are also overlapping at times as websites can be accessible both through desktop, laptop and smartphones.

(6) Specialty Media: These consist of items that are given away to the consumer on which the name of the company or brand is printed so that more people get to know about it. For example-carry bags, membership cards, free merchandise like caps or bags, etc. These type of advertising media are more niche and have a narrow reach as compared to the above mentioned media.

(7) Other forms: Apart from the ones discussed above, advertising can be done through transit signs i.e. the small posters that we see on trains or buses, electronic billboards, etc. Some ads can be advertised before the movies in cinema halls as well, where it can reach out to a large group of similar audience in terms of demography or geography.

Requisite of an ideal medium:

For companies, it is important to have a clear cut plan in the selection of advertising media. Some steps followed in advertising media selection are:

(1) The objective of the company is analysed as to what product and to which customers it is to be advertised.

(2) The next stage is to have a complete understanding about the customer demographics who are to be targeted.

(3) After that, depending upon the type of product, type of customers, the advertising budget set, companies can choose from the various types of

advertising media. Advertising media should be chosen on the fact which gives maximum return on investment. Companies should spend minimum on advertising, reach out to as many people as they can and which should convert into substantial sales to give profit to the company.
(4) Over a period of time, this processing of selecting the appropriate advertising media can be repeated for increasing cost benefit to the company.
For every type of advertising media, there are different parameters based on which they can be measured:
(1) For a print or a TV/radio ad, a phone number or email can be given for customers to contact the company if they want, and through the number of people who have tried to contact, we can measure the impact of the ad.
(2) For an internet ad which is placed on different website homepages, if the company or brand has an online website too, the number of clicks which direct the customers to the company website measures the impact of the ad. But if the company does not have a website, contact information can be displayed on the banner as in the case of print ads, and the impact can be measured similarly.

Q3. What are the various modes of creating charge? Explain them briefly.
Ans. Refer to Chapter-4, Q.No.-8 (Pg. No.-104)

Q4. What is a 'Public Corporation'? Explain its merits and limitations.
Ans. Refer to June-2005, Q.No.-5 (Pg. No.-172)

Q5. What is a joint stock company? Explain its limitations as a form of business organisation.
Ans. Refer to Chapter-1, Q.No.-17 and Q.No.-11 (Pg. No.-27, 18)

Q6. Write shorts notes on any two of the following:
(a) Aids to trade
Ans. Refer to Chapter-1, Q.No.-4 (Pg. No.-5)

(b) Money market
Ans. Money Market can be understood as the market for short term funds, wherein lending and borrowing of funds varies from overnight to a year. It is an important part of the financial system that helps in fulfilling the

short term and very short term requirements of the companies, banks, financial institution, government agencies and so forth.

In this market, only those financial instruments are traded which are immediate substitutes for money, which includes:

(1) Call/Notice Money: When the money raised or borrowed on demand for a very short term which ranges from one day to 14 days, then it may be called as notice money, and when it exceeds 14 days it is termed as call money.

(2) Treasury Bills: These are short term, negotiable financial assets issued by the central bank, on behalf of the government, for overcoming liquidity shortfalls.

(3) Commercial Bills: A commercial bill is a negotiable, self-liquidating instrument that is less risky in nature. When goods are bought on credit, these bills improve the liability to make payment at the specified date.

(4) Commercial Paper: It alludes to an unsecured promissory note, issued by large and creditworthy companies, at a discount on its face value and redeemable at its face value.

(5) Certificate of deposit: It is an unsecured, negotiable financial instrument which a bank and financial institution issues to individuals, corporation, trust, funds etc. at a discount on its face value and its maturity vary from 15 days to one year.

The financial assets dealt in the money market possess high liquidity, low transaction cost, less risky and no loss in value. And so, it acts as a whole sale debt market for such instruments.

(c) Channel of distribution

Ans. Refer to Chapter-3, Q.No.-7 (Pg. No.-72)

(d) Procedure of Import trade

Ans. Refer to Chapter-3, Q.No.-16 (Pg. No.-85)

ECO-1: BUSINESS ORGANISATION
December, 2018

Note: Attempt both Part-A and Part-B.

PART - A

Q1. Attempt any four of the following:

(a) Enumerate the essentials of an effective advertisement.

(b) Briefly explain the services provided by retailers to consumers.

(c) List out the factors affecting the capital structure of a firm.

(d) Distinguish between 'Entrepreneur' and 'Promoter'.

(e) Explain the benefits of containerisation for transportation of goods.

(f) State the features of public utilities.

PART - B

Attempt any three questions:

Q2. Explain the financial performance of public enterprises in India.

Q3. "All business risks are not insurable". In the light of this statement, explain insurable risks and non-insurable risks.

Q4. Define the term 'business' and explain its essential features.

Q5. Describe 'factoring' and 'discounting of bills of exchange' as methods of raising short-term finance.

Q6. Explain the objectives of advertising.

Q7. (a) Discuss how does a letter of credit help in financing foreign trade.

(b) Narrate the shipping documents required to be submitted along with a documentary letter of credit.

ECO-1: BUSINESS ORGANISATION
June, 2019

Note: Attempt any five questions. All questions carry equal marks.

Q1. Distinguish between the following:
(a) Ownership capital and Borrowed capital.
Ans. Refer to June-2007, Q.No.- 1(d) (Pg. No.-188)

(b) Business and Commerce
Ans. Refer to Chapter-1, Q.No.-1 and Q.No.-4 (Pg. No.-1, 4)

Q2. Explain the concept of 'Business' and describe the objectives of business.
Ans. Refer to Chapter-1, Q.No.-1 (Pg. No.-1)

Q3. What is cooperative form of business organisation? Explain the features of a cooperative form of organisation.
Ans. Refer to Chapter-1, Q.No.-11 (Pg. No.-17)

Q4. What are the various types of business risks? Discuss the various steps involved in risk management.
Ans. Refer to Chapter-4, Q.No.-9 and Q.No.-10 (Pg. No.-106, 108)

Q5. What is a public utility? Explain its features.
Ans. Refer to Chapter-5, Q.No.-9 (Pg. No.-143)

Q6. Outline the factors which influence the choice of distribution channel.
Ans. Refer to Chapter-3, Q.No.-8 (Pg. No.-71)

Q7. Discuss various methods of raising short-term capital.
Ans. Refer to Dec-2016, Q.No.-13 (Pg. No.-231)

Q8. Explain the relationship between a banker and its customer.
Ans. Refer to Chapter-4, Q.No.-3 (Pg. No.-95)

ECO-1: BUSINESS ORGANISATION
December, 2019

Note: Attempt any five questions. All questions carry equal marks.

Q1. What is capital structure? State the various factors responsible for deciding the capital structure of a company.

Q2. Distinguish between Entrepreneur and Promoter. Explain the characteristics of an Entrepreneur.

Q3. What is foreign trade? Write its importance and common problems of foreign trade.

Q4. Mention the concept of channel of distribution. What are the various factors affecting the choice of the distribution channel? Explain.

Q5. Distinguish between the following:
(a) Partnership and Company
(b) Equity shares and Preference shares

Q6. Write short notes on the following:
(a) Rationale of public enterprises
(b) Trade credit

Q7. "Advertisement is a social waste." Comment.

Q8. Explain the factors determining the choice of the form of business organization.

ECO-1: BUSINESS ORGANISATION
June, 2020

Note: Attempt both Part-A and Part-B.

PART A

Q1. Attempt any four of the following:
Differentiate between:
(a) Business and commerce
(b) Capital market and money market
(c) Intensive distribution and exclusive distribution
(d) Government Enterprise and Public Limited Company
(e) Super market and Departmental store
(f) Equity shares and preference shares.

PART B

Attempt any three of the following questions:
Q2. Mention various prerequisites for deciding an ideal form of Business Organisation?

Q3. What is 'Capital Structure'? What are the various factors determining the capital structure?

Q4. Write short notes on any two of the following:
(a) Distinction between Entrepreneur and Intrapreneur
(b) Factoring
(c) Foreign sources for raising capital
(d) Arguments against advertising

Q5. What do you understand by 'Bank'? Explain various types of banks.

Q6. Explain sea transportation Tabulate its classification based on area of operation? Mention its procedure?

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Ken Blanchard

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