BUSINESS STUDIES

FIRST YEAR FOCUS AREA NOTES

ENGLISH

PREPARED BY

VINOD E B , O L L H S S, UZHAVOOR, KOTTAYAM

MOB: 9544 389 770

CHAPTER 1

Business, Trade and Commerce

Business

Business refers to an occupation in which people regularly engage in activities related to purchase/ production and sale of goods and services with a view to earning profit.

Characteristics of business

1.An economic activity

Business is considered to be an economic activity because it is undertaken with the object of earning money

2. Production or procurement of goods and services

Every business enterprise either produces goods on its own or assembles them from producers to be sold to consumers.

3. Sale or exchange of goods and services

Business involves transfer or exchange of goods and services for some consideration. Eg: cooking food at home for the family is not business, but cooking food and selling it to others in a restaurant is business.

4. Dealings in goods and services on a regular basis

Business involves dealings in goods or services on a regular basis. One single transaction of sale or purchase does not constitute business. Eg: if a person sells his domestic radio ,it is not business. But if he sells radio sets regularly through a shop, it is business.

5. Profit earning

One of the main purpose of business is to earn income by way of profit.

6. Uncertainty of return

It is not certain as to what amount of profit will the business earn in future. There is always a possibility of losses being incurred.

7. Element of risk

There is an element of risk in every business. No business can altogether avoid risks.

Classification of business activities

Business is classified into two categories

A. Industry and B. Commerce

Industry

Industry refers to economic activities, which are concerned with the conversion of resources in the useful goods. Industries are again classified into 3. 1. Primary 2. Secondary and 3.Tertiary

1. Primary industry

It includes all those activities which are concerned with extraction and production of natural resources and reproduction and development of living organisms and plants. They are further sub-divided into

a) Extractive industries

These industries are engaged in the extraction or production of products from soil, water etc. Eg: fishing, mining, hunting, farming etc.

b) Genetic industries

These industries are engaged in producing, breeding or multiplying of certain species of animals or plants. Eg: cattle breeding, poultry farming, nurseries, forestry etc.

2. Secondary industry

These industries process the materials extracted at the primary stage to produce goods for final consumption or for further processing. These are further subdivided into

a) Manufacturing industries

These are concerned with the conversion of raw materials into finished goods. Eg: cotton into textile, timber Indo furniture, iron ore into steel etc. These industries are divided into 4

i) Analytical industry- this industry separates different elements from the same material Eg: oil refinery

ii) Synthetical industry- This Industry combines various ingredients Indian new products. Eg: cement

iii) Processing industry- It involves successive stages for manufacturing of finished products. Eg: sugar, paper etc.

iv) Assembling industry- This Industry assembles different components into a new

product. Eg: computer, car, TV etc.

b)Construction industries

These industries are engaged in the construction of roads, buildings, dams, bridges etc.

3. Tertiary Industry

These are concerned with providing support services to primary and secondary industries. Transportation, banking, insurance, warehousing, communication etc. come under this category.

Commerce

Commerce Is the sum total of those activities which are engaged in the removal of hindrances of person, place and time in the exchange of commodities.

Commerce includes a) Trade and b) Auxiliaries or aids to trade.

Trade

Trade means buying and selling of goods. It helps the movement of goods from the producers to consumers. Trade removes the hindrance of person

Types of trade

1. Home trade (Internal or domestic trade)
2. Foreign trade (external or International trade)

Home trade

Home credit is concerned with buying and selling of goods and services within the geographical boundaries of a country. This is further classified into two viz, wholesale trade and retail trade

a) Wholesale trade

It involves buying goods from producers in large quantities and selling them to retailers in small quantities

b) Retail trade

It involves buying goods from wholesalers and selling them to consumers in relatively small quantities.

Foreign trade

It consists of trade among different nations. It is further divided as follows

a) Import Trade

If goods are purchased from a foreign country, it is called import trade.

b) Export trade

If goods are sold to foreign countries, it is called export trade

c) Entrepot trade

When goods are imported from a foreign country to export them to other countries. it is called entrepot trade.

Auxiliaries to trade(Aids to trade)

Activities which are meant for assisting trade are known as aids to trade

1. Transportation

It facilitates the movement of raw materials to the place of production and the finished goods from factories to the place of consumption. It removes the hindrance of place

2. Banking

Business requires funds for acquiring assets, purchasing raw materials and meeting day to day expenses. Banks provide the necessary funds to business. So hindrance of finance is removed by banking

3. Insurance

In business, there are many risks like destruction of property by fire, flood, earthquake etc. Insurance provides protection in all such cases. It removes the hindrance of risk

4 .Warehousing

Goods are not sold immediately after production. They are to be stored until they are sold. Warehousing helps the business to overcome the problem of storage. It removes the hindrance of time

5. Advertising

It provides information about the available goods and services such as their price, uses, quality etc It induces customers to buy particular items. It removes the hindrance of Knowledge.

CHAPTER 2

FORMS OF BUSINESS ORGANISATION

Sole proprietorship

A business concern owned and managed by a single person is called as sole proprietorship. It is also called as sole trader or one man business.

Features

1. Formation and closure

It can be easily started by anyone as there are no legal formalities.

2. Liability

A Sole trader has unlimited liability. That is he is personally liable for the debts of the firm in case the assets of the business are not sufficient to meet all the debts.

3. Sole risk bearer and profit receipient

He alone has to bear all the business risks and he is is the sole recipient of all the profits.

4. Control

The right to run the business and make all decision lies absolutely with the sole trader

5. No separate entity

The business does not have an identity separate from the owner. That is, no distinction is made between the owner and his business.

6. Lack of business continuity

The death, insanity, insolvency, imprisonment etc of the owner may lead to closure

of business.

Merits

1. Quick decision making

As there is no need to consult others, a sole trader can take quick decisions.

2. Confidentiality of information

A sole trader can keep all the information related to business operation confidential.

3. Direct incentive

Sole trader is the sole recipient of all profit of business. This provides maximum incentive to be sole trader to work hard.

4. Sense of accomplishment

A sole trader works for himself. The success of his business create self confidence and a sense of accomplishment in him.

5. Ease of formation and Closure

It is easy to start and close the business as per the wish of the owner.

Limitations

1. Limited resources

The financial resources of a sole trader is limited to his personal savings and borrowing from others. Banks and other lending institutions hesitate to give long- term loans to sole trader.

2. Limited life

Death, Insanity or illness of sole trader affects business and can lead to its closure.

3. Unlimited liability

As the liability of a sole trader is unlimited, he has to use his personal asset to pay of the debts of the firm if the business assets are insufficient to pay off business debts.

4. Limited managerial ability

A sole trader may not have all the managerial ability to conduct the business

PARTNERSHIP

The Indian Partnership Act 1936 defines Partnership as " the relation between persons who have agreed to share the profits of the business carried on by all or any one of them acting for all".

Features

1.Formation

The partnership is formed by an agreement between persons. It is governed by the Indian Partnership Act 1932.

2. Liability

The liability of partners is unlimited

3. Risk bearing

The partners bear the risks involved in running a business as a team.

4. Decision making and control

The decision making responsibility and controlling the business are shared by the partners.

5. Continuity

There is lack of continuity of business since the death, retirement or insanity of any partner may lead to reconstitution of partnership.

6. Membership

The minimum number of members needed to start a partnership firm is two. The maximum number is 10 in case of banking business and 20 in case of other businesses.

7. Mutual agency

Every partner is both an agent and principal. He is an agent when he binds others through his acts and he is a principal when he is bound by the acts of other partners.

Partnership deed

It is necessary to have an agreement to form a partnership. Such agreement may be oral or written. The written agreement among partners which specifies the terms and conditions of partnership is called partnership deed.

Contents of partnership deed

1. Name of firm

2. Name and address of partners

3. Nature and location of business

4. Duration of business

5. Capital contributed by each partner

6. Profit sharing ratio

7. Rights and duties of partners

8. Salaries of partners

9. Interest on capital and interest on drawings.

10. Preparation of accounts and their audits

11. Procedure for dissolution of the firm.

Co-operative society

The co-operative society is a voluntary association of persons , who join together with the motive of welfare of the members. Registration of a co-operative society is compulsory under the Co-Operative Societies act 1912.There must be at least 10 adult persons to form a society.

Features

1. Voluntary membership

A person is free to join a society and can also leave anytime as per his desire.Membership is open to all , irrespective of their religion, caste and gender.

2. Legal status

Registration of a co-operative society is compulsory. It has a separate legal entity apart from its members. It can enter into contract, and purchase property in its own name, sue and be sued by others.

3. Limited liability

The liability of the members is limited to the amount of capital contributed by members

4. Control

The control of a co-operative society is vested with a managing committee elected from among the members

5. Service motive

The objective of a co-operative society is to render service to its members and not making profit

Joint Stock Company

A company is an association of many persons who contribute money or money's worth to a common stock and employs it in some trade or business and who share the profit or loss arising there from.

A company can be described as an artificial person having a separate legal entity, perpetual succession and a common seal.

It is governed by the Indian companies Act 1956. The capital of a company is divided into a number of units of equal value. One such unit is called a share. The person who takes up shares is called shareholder and shareholders are the owners of the company.

Features

1. Artificial person

A company is an artificial person created by Law. It is an incorporated association registered under the Companies Act.

2. Separate legal entity

On registration a company acquires an identity distinct from its members . It can own property, sue and be sued in its own name.

3. Formation

A company is formed through registration under the Indian Companies Act 1956. Registration is compulsory for joint stock companies.

4. Perpetual succession

A company being a creation of the Law, can be brought to an end only by Law. Members may come and members may go, but the company continues to exist. The death, insolvency or insanity of members will not affect its existence.

5. Control

The management and control of a company is vested with the Board of Directors. They are elected from among the shareholders in their general meeting.

6. Liability

The liability of members is limited to the extent of capital contributed by them in a company. That is the personal property of the members cannot be used to pay off debts of the company.

7. Common seal

As a joint stock company is an artificial person, it cannot sign documents for itself.So a common seal with the company's name is used for its signature.

Private company

A Private company is a company which by its Articles

a) restricts the right of members to transfer its shares

b) has a minimum of 2 and a maximum of 200 members

c) does not invite public to subscribe to its share capital

A private company must add the word 'Private Limited' after its name. If a private company contravenes any of the above said provisions , it ceases to be a private company and loses all its privileges.

Public Company

As per Indian Companies act, a public company is one which,

1) has a minimum of 7 members and no limit on maximum members.

2) has no restriction on transfer of shares.

3) is not prohibited from inviting the public to subscribe to its capital

Differences between a public company and A private company

Basis	Public company	Private company

1.Members	**Min-7** **Max- No limit**	**Min- 2** **Max – 200**
2.Minimum no.of directors	**3**	**2**
3.Index of members	**Compulsory**	**Not compulsory**
4. Transfer of shares	**No restriction**	**Restriction on transfer**
5.Prospectus	**Can issue prospectus**	**Cannot issue prospectus**

CHAPTER 4

BUSINESS SERVICES

Commercial banks

Commercial banks are institutions dealing in money. They are governed by Indian Banking Regulation act 1949. There are two types of Commercial banks :-

a) Public sector banks

Public sector banks are those in which the govt has a major stake. They emphasis on social objectives rather than profitability. Eg: SBI, PNB, IOB, Canara Bank etc

b) Private Sector banks

Private Sector banks are owned, managed and controlled by private promoters. They emphasis more on profitability. Eg: HDFC, ICICI, Kotak Mahindra etc.

Functions of Commercial banks

The important functions of commercial banks are discussed below

1. Acceptance of deposits

An important function of a commercial bank is to accept money from the public as deposit. Banks lend money out of the deposits received from public. Important types of deposits are

a) Current account

It is suitable for businessman. Any amount of money can be deposited at any number of times. But money can be withdrawn subject to the fund available

b) Savings bank account

Savings accounts are for promoting savings by individuals. Banks pay rate of interest as decided by RBI. A person can deposit any amount of money at any number of times. But there are certain restrictions as to the amount and number of withdrawals from this account.

c) Fixed or Time deposit

These are deposits made for a fixed period of time say, 1 year, 3 years, 5 years etc. They carry a higher rate of interest than savings deposit. Premature withdrawal is permissible with a percentage of interest being forfeited.

2. Lending of funds

Another important function of commercial banks is to provide loans to customers. These may be in the form of loans, overdrafts, cash credits, consumer credits, discounting trade bills etc.

3. Cheque facility

Banks help customers by collecting their cheques drawn on other banks. Cheque can be used to make payments and withdraw money. There are two types of cheques, namely

a) Bearer cheque- encashable immediately at bank counters.

b) Crossed cheque- are deposited only in the Payee's account.

4. Remittance of funds

Banks provide the facility of fund transfer from one place to another. If a person wants to send some amount to another person at distant places, he can buy a Demand Draft (DD) from a bank. The bank draws a DD on its own branches or other banks at those places. The DD is then sent to the payee by post. The Payee can present the DD on the drawee bank at his place and collect the amount.

5. Allied services

Banks also provide allied services like bill payments, locker facilities, buying and selling of shares, payment of rent, insurance premium, collection of dividend etc.

E- Banking

E-Banking means electronic banking or banking using electronic media. It is a service provided by banks,that allows a customer to conduct banking transactions, such as managing savings, checking accounts, applying for loans or paying bills over the internet using a Personal computer or Mobile Phone. The services include Electronic Fund Transfer(EFT), Automated Teller Machine (ATM), Debit Card, Credit Card, Digital cash etc.

Benefits

To customers

1. It provides 24 hour a day, 365 days a year service to the customers.

2. Customers can make some transactions from office or house or while travelling via mobile phone

3. It creates a sense of financial discipline.

4. Less risk and greater security to the customer as they can avoid travelling with cash.

To banks

1. It provides competitive advantage to the bank.

2. Load on branches can be considerably reduced.

Insurance

It is a contract under which one party agrees in return for a consideration to pay and agreed amount of money to another party to make good a rose, damage or injury do something of value in which the insured has a pecuniary interests as a result of some uncertain event.

There are two parties two insurance namely insured and insurer.

Insured

The person whose life or property is insured against risk is called insured

Insurer

The firm which insures the risk of loss is called insurer.

Premium

The consideration paid by the insured to the insurer to compensate the loss is called premium

Policy

The written document containing the terms and conditions of insurance is called policy

Subject matter

The life or property insured is called subject matter

Principles of insurance

1. Utmost good faith

Insurance is a contracts of uberimae fidei ie , a contract of utmost good faith. Both the insurer and the insured should display good faith towards each other. The insured should make full disclosure of all material facts concerning the subject matter to the insurer. The insurer should make clear all the terms and conditions in the policy to the insured.

2. Insurable interest

The insured should have an insurable interest in the subject matter of insurance. Insurable interest means pecuniary interest. A person is said to have insurable interest in the subject matter if he stands to benefit by its safety and suffers financial loss by its damage or loss.

3. Indemnity

Indemnity means to make good the loss. It means that the insurer will pay only the actual amount of loss not exceeding the amount of policy. That is the insured is not allowed to make profit out of insurance. This principle is not applicable to Life Insurance.

4. Proximate course(causa proxima)

Proximate cause is the direct course for the loss. When there are two or more causes for a loss, the principle of proximate cause is applied. The insurer is liable to pay compensation to the insured if the loss is caused by a peril insured against.

5. Subrogation

After settlement of the claim, the insurer stands in the place of insured. That is the right of ownership of the subject matter is passed on to the insurer after the claim is settled. The insured cannot make profit by selling the damaged property.

6. Contribution

This principle applies to all Double Insurance contracts. In case of Double Insurance, the insurers should share the losses in proportion to the policy amount. That is, the insured can recover only the actual amount of loss from all the insurance together.

7. Mitigation

This principle states that it is the duty of the insured to take reasonable steps to minimise the loss or damage to the insured property. He should not become careless when the mishap occurs by thinking that the subject matter is insured and the insurer will pay compensation.

Warehousing

Warehouse is a place where goods are stored in anticipation of future demand.

Types of warehouses

1. Private warehouses

Private warehouses are owned and operated by big business concerns for storing their goods.

2. Public warehouses

These can be used for storage of goods by traders or any member of the public by paying a storage fee. The government regulates the operations of these warehouses by issuing licenses for them to private parties .

3. Bonded warehouse

These warehouses are licensed by the government to store imported goods until customs duty is paid . They are located near ports. Goods can be removed in part as and when required by the importers and import duty can be paid in instalments.

4. Government warehouse

These are warehouses which are fully owned and managed by the government.eg: Food Corporation of India, State Trading Corporation and Central Warehousing Corporation.

5. Co-operative warehouses

Some marketing cooperative societies or agricultural cooperative societies have set up their own warehouses for their members.

CHAPTER 5

EMERGING MODES OF BUSINESS

E- business

E- business may be defined as the conduct of industry, trade and commerce using the computer networks e- business and e- commerce are not same. e- business is a broad term and includes e- commerce. e-Commerce means buying and selling of goods online. But e- business includes not only e-commerce but also other functions like production, inventory management, product development, accounting, Human Resource Management etc.

Scope of e-business

1 B2B Commerce

Transaction taking place between business enterprises electronically is called B2B transaction.eg: placing order with supplier

2. B2C Commerce

This is a transaction taking place between business and consumer. eg:consumer places an order online

3.Intra-B Commerce:

Here, parties involved in the electronic transactions are from within a given business firm.Eg: Communication between Marketing and Production Department

4. C2C Commerce

This is a transaction taking place between a consumer and another consumer Eg: OLX

Differences between traditional and e-business

Basis	Traditional business	e-Business
1. Ease of formation	Difficult	Simple
2. Physical presence	Required	Not required
3. Operating cost	High	Low
4. Opportunity for Inter personal touch	Much more	Less
5. Setting up cost	High	Low
6. Business expansion	Difficult	Very much possible
7. Physical examination of good	Possible	Not possible
8. Nature of contact between buyer and seller	Direct *	indirect *

Business Process Outsourcing (BPO)

It is a system of getting business tasks accomplished through an outside agency

Features

1. It involves contracting out

Some works of a business are given to outside agencies on a contract basis.eg: a hospital contracts out sanitation work to an outside agency.

2. Non-core business activities are outsourced

Only the non-core activities of the business are outsourced to outside agencies.eg: a school contracts out the work of running canteen for its students.

3. Processes may be outsourced to a captive unit.

If the task of performing some activity internally is very large , it is beneficial for a company to have a captive service provider ie, a service provider set up for providing services to only one firm.

Need for outsourcing (Benefits)

1. Focusing of attention

It enables the business to concentrate on areas in which it has core competency.

2. Quest for excellence

Business firms can excel by contracting out their non-core activities to those who excel in performing them.

3. Cost reduction

A business can reduce its operating cost by outsourcing some activities to agencies who are specialised in these activities.

4. Growth through alliance

A firm doesn't have to make investment in activities which are outsourced. So it can grow with minimum investment.

5. Fillip to economic development

Outsourcing stimulates entrepreneurship, employment and export. These lead to economic development.

CHAPTER 6

SOCIAL RESPONSIBILITY OF BUSINESS AND BUSINESS ETHICS

Social responsibility is the obligation of a business to take those decisions and perform those actions which are desirable in terms of the objectives and values of our society.

Arguments for social responsibility

1. Justification for existence and growth

The prosperity and growth of business is possible only through continuous service to society. So, assumption of social responsibility is necessary for its existence and growth.

2. Long-term interest of the firm

When members of society ie, workers, consumers, govt etc. feel that business enterprise is not serving their interest, they will withdraw their co-operation to the enterprise. So, it is in the interest of business to assume social responsibility.

3. Avoidance of govt regulation

Govt regulations are undesirable because they limit freedom. Businessman can avoid the problem of govt regulation by voluntarily assuming social responsibility.

4. Maintenance of society

People who feel that they are not getting their due from the business may resort to anti-social activities. So, it is desirable that business assumes social responsibility.

5. Availability of resources with business

Business enterprises have valuable financial and human resources. These can be effectively used for solving social problems.

6. Better environment for doing business

If business is to operate in a society which is full of complicated problems, it may have little chance of success. A society with fewer problems provides better environment for a firm to conduct its business.

7. Holding business responsible for social problems

It is argued that some of the social problems are created by business firms such as environmental pollution, unsafe workplace etc. So, it is the moral obligation of business to solve these problems.

Arguments against social responsibility

1. Violation of profit maximisation objective

According to this argument, business exists only for profit maximisation. So, any talk of social responsibility is against this objective.

2. Burden on consumers

Social responsibility like pollution control and environmental protection are very costly. In such circumstances, businessmen are likely to shift their burden to consumers by charging higher prices from them.

3. Lack of social skills

Businessman do not have the necessary understanding and training to solve social problems. Therefore, social problems should be solved by other specialized agencies.

4. Lack of broad public support

Public in general doesn't like business involvement in solving social problems.

Kinds of social responsibility

1. Economic responsibility

A business enterprise is basically an economic entity and therefore, its primary social responsibility is economic. That is, produce goods and services that society wants and sell them at a profit.

2. Legal responsibility

Every business has a responsibility to operate within the laws of the land. A law abiding enterprise is a socially responsible enterprise as well.

3. Ethical responsibility

This includes the behaviour of the firm that is expected by society but not codified in law. Eg: following fair trade practices, providing quality goods to consumers etc.

4. Discretionary responsibility

It refers to purely voluntary obligation that an organisation assumes. Eg: providing charity to educational institutions, helping affected people during flood or earthquakes etc.

Social responsibility towards different interest groups

1. Responsibility towards shareholders or owners

A business enterprise has the responsibility to provide a fair return to the shareholders or owners on their investment and to ensure the safety of their investment. It should also give accurate and full information about its working to the owners.

2. Responsibility towards the workers

A business enterprise should create good working conditions in the working place, give good wages to the workers, respect the democratic rights of the workers to form unions etc.

3. Responsibility towards the consumers

A business enterprise should supply right quantity and quality goods and services to consumers at reasonable prices. It should not indulge in adulteration, misleading advertisement, providing poor quality goods etc.

4. Responsibility towards the Govt and community

A business enterprise must respect the laws of the country and pay taxes regularly and honestly. It must protect the environment and avoid dirty working conditions

Business and environmental protection

Environment is defined as the totality of man's surroundings- both natural and man made. The activities of business cause environment pollution

Pollution

Pollution means the injection of harmful substances into the environment. Pollution harms human life and the life of other species.

Types of pollution

1. Air pollution

It is mainly due to carbon monoxide emitted by automobiles. Similarly, smoke and other chemicals from manufacturing plants also pollute air. Air pollution lowers the quality of air.

2. Water pollution

Water becomes polluted from chemicals and waste dumping. It leads to the death of several animals and pose a serious threat to human life.

3. Land pollution

Dumping of toxic wastes on land causes land pollution. This damages the quality of land and makes it unfit for agriculture.

4. Noise pollution

Noise caused by the running of factories and vehicles is also a serious health hazard. Noise pollution is responsible for many diseases like loss of hearing, malfunctioning of heart, and mental disorder.

CHAPTER 7

FORMATION OF A COMPANY

Formation of a company involves FOUR distinct stages ; which are

A) Promotion B) Incorporation C) Subscription of capital D) Commencement of business

A] Promotion

Promotion is the first stage in the formation of a company. It means the sum total of all activities which are necessary for bringing the company into existence. Person who takes the initiative to form a company is called promoter.

Functions of a promoter

1. Identification of business opportunity

The first function of a promoter is to identify a business opportunity. The opportunity may be in respect of producing a new product or service or making some product available through a different channel etc.

2. Feasibility studies

The promoter then undertakes a detailed feasibility study to investigate all aspects of the business idea. It involves the following

a) Technical feasibility

Sometimes an idea may be good but technically not feasible to execute. It may be so because the required technology is not easily available.

b) Financial feasibility

The promoter has to find out the fund requirement of the identified business opportunity. If the funds required for the project cannot be easily arranged, the project has to be given up.

c) Economic feasibility

The promoter has to analyse the profitability of the proposed project. He takes the help of experts to conduct these studies.

3. Name approval

After deciding the project, the promoter has to select a name for the company. He then submits an application for name approval to the Registrar of Companies of the State in which the registered office of the company is to be situated. Three names in the order of their priority are given in the application to the Registrar.

4. Fixing up signatories to the Memorandum of Association

Promoters have to decide the members who have to sign the Memorandum of Association of the proposed company. The people signing the memorandum are also the first directors of the company.

5. Appointment of professionals

Certain professionals such as Merchant Bankers, Auditors etc. are appointed by promoters to assist them in the preparation of necessary documents to be filed with the Registrar.

6. Preparation of necessary documents

The promoter takes steps to prepare certain legal documents to be filed with the Registrar. These include Memorandum of Association, Articles of Association and consent of directors.

Memorandum of Association:

It is the most important document of a company. It defines the objectives and powers of a company. It describes the relationship of the company with the outsiders. Memorandum of Association is called the Charter or Magna Carta of a company.

Contents or clauses of Memorandum of Association

Memorandum of Association has SIX clauses which are stated below.

1. Name clause

This clause contains the name of the company with which it is registered. The name should not be similar with the name of an existing company. The name of the company should be exhibited outside its office and should be shown on all its bills, letters, notices etc.

2. Registered office (Domicile) clause

This clause contains the name of the state in which the registered office of the company is proposed to be situated.

3. Objects clause

It defines the objectives for which the company is formed. A company cannot undertake an activity which is beyond the objects stated in this clause.

4. Liability clause

This clause limits the liability of the members to the amount unpaid on the shares owned by them. Eg: if a person purchased 100 shares of Rs.10 each and has already paid Rs.7 per share, his liability is limited to Rs. 3 per share.

5. Capital clause

This clause specifies the maximum capital which the company is authorised to raise through the issue of shares. The authorised capital of the company along with its division into the number of shares having a fixed face value is specified in this clause.

6. Association clause

In this clause, the persons who signed the Memorandum of Association state their intention to be associated with the company and also give their consent to purchase qualification shares.

Articles of association

It is a document containing the rules regarding the internal management of a company. These rules are subsidiary to the Memorandum of Association.

A public company needs not have its own articles. It may adopt Table A , which is a model set of articles given in the Companies Act.

The Articles generally contains the following matters

1. Number and value of shares.

2. Issue of preference shares.

3. Allotment of shares.

5. Transfer of shares.

6. Forfeiture of shares.

7. Alteration of capital.

8. Buy back.

9. Share certificates.

10. Voting rights

11. Meetings and rules regarding committees.

12. Directors, their appointment and delegations of powers.

13. Issue of Debentures and stocks.

14. Seal.

15. Remuneration of directors.

16. General meetings.

17. Directors meetings.

18. Winding up.

Differences between Memorandum of Association and Articles of Association

Basis	Memorandum of Association	Articles of Association
1. Objectives	It defines the objectives for which the company is formed	It contains the rules for internal management of the company
2. Position	It is the main document	It is a subsidiary document
3. Relationship	It defines the relationship of the company with outsiders	It defines the relationship of the company and its members

4.Necessity	**Every company has to file Memorandum**	**It is not compulsory for a public company to file Articles**
5.Alteration	**Alteration of Memorandum is very difficult**	**Articles can be altered by a special resolution**

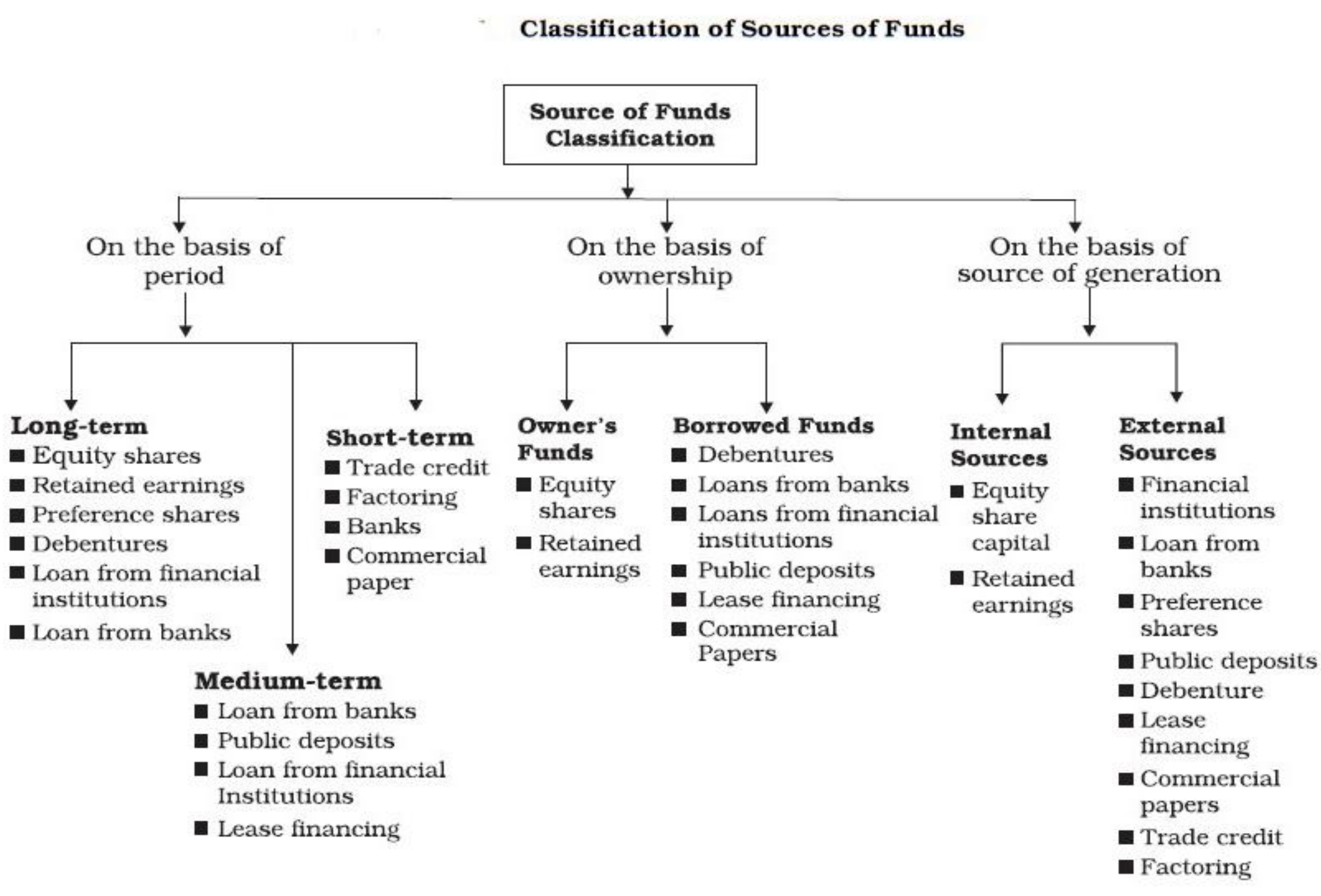
Prospectus

Prospectus is an invitation to public to apply for shares or debentures of the company or to make deposits in the company. A prospectus should be filed with the Registrar of Companies to raise funds.

CHAPTER 8

SOURCES OF BUSINESS FINANCE

Classification of sources of finance



A] On the basis of period

1. Long-term finance- Funds required for a period exceeding 5 years

2. Medium-term finance- Funds required for a period exceeding one year but less than 5 years.

3. Short-term finance- Funds required for a period not exceeding one year.

B] On the basis of ownership

1. Owner's funds- Funds provided by the owners of the enterprise.

2. Borrowed funds- Funds raised through loans and borrowings.

C] On the basis of source of generation

1. Internal sources- Funds generated from within the business.

2. External sources- Funds generated from outside the business.

Retained earnings

The portion of profit which is retained in the business for future use is called retained earnings. It is also called ploughing back of profit or internal financing or self-financing.

Merits

a) It is a permanent source of funds.

b) No cost involved in raising funds

c) No security is needed to raise funds.

d) It makes company financially strong.

e) It helps the company to meet unexpected losses.

Limitations

a) Excessive ploughing back may cause dissatisfaction among shareholders.

b) It is an uncertain source of funds as the profits of business are fluctuating

c) It may be used for tax evasion

Issue of shares

The capital obtained by issue of shares is called share capital. The person holding shares is called shareholder. There are two types of shares namely Preference shares and Equity shares.

a) Preference shares

Shares which carry preferential rights in receiving a fixed rate of dividend and repayment of capital on winding up of the company is called preference shares. Preference shareholders have voting rights only on matters affecting them.

Merits

a) As the rate of dividend is fixed, these shares provide a steady income.

b) These shares are suitable for investors who want a regular income with low risk.

c) It doesn't dilute the control of equity shareholders over the management of the company.

d) These can be redeemed if needed.

e) These shares do not create any charge on the assets of the company.

Limitations

a) These are not suitable for investors who are willing to take risk.

b) The rate of dividend on preference share is higher than the rate of interest on debentures.

c) The dividend paid is not deductible from profits as expense.

Types of preference shares

i) Cumulative and non-cumulative

Cumulative preference shareholders will be paid arrear dividend in future years , if no dividend is paid in any year.

Non- cumulative preference shareholders will not get their arrear dividend, but only current years dividend.

ii) Participating and non-participating

Participating shareholders have a right to share the surplus profits after a fixed rate of dividend is paid to equity shareholders.

Non-participating shareholders have no right to share surplus profits, but will get only dividend at a fixed rate.

iii) Redeemable and irredeemable

Preference shares which will be repaid after the expiry of a specified period are called redeemable preference shares.

Preference shares which will be repaid only on winding up of the company are called irredeemable preference shares.

iv) Convertible and non-convertible

Preference shares that can be converted into equity shares within a specified period of time are known as convertible preference shares.

Preference shares that cannot be converted into equity shares are known as non-convertible preference shares.

Equity shares

Shares without any preferential right in payment of dividend and repayment of capital are called equity shares. Equity shareholders are the real owners of the company and thus the capital raised by issue of such shares is called ownership capital. They have the right to vote and participate in the management of the company.

Merits

a) Equity shares are suitable for investors who are willing to take risk.

b) Payment of dividend to equity shareholders is not compulsory.

c) Equity capital is a source of permanent capital.

d) Equity shares don't create any charge on the assets of the company.

e) Equity shareholder can participate in the management of the company.

Limitations

a) Investors who want steady income may not prefer equity shares.

b) More formalities are involved in the issue of equity shares.

c) These shares cannot be normally redeemed.

Debentures

A debenture is an acknowledgement that the company has borrowed a certain sum of money ,which it promises repay at a future date. Debenture holders are the creditors of the company. They get a fixed rate of interest at specified intervals say 6 months or one year.

Merits

a) It is preferred by investors who want fixed income.

b) Debenture holders need not be paid share of profit of company.

c) It is suitable when company's earnings are stable.

d) As Debenture holders don't have voting right, it doesn't dilute control of equity shareholders on management.

Limitations

a) As the rate of interest is fixed, it puts a permanent burden on the earnings of a company.

b) With issue of debentures, the capacity of a company to further borrow funds reduces.

Types of debentures

i) Secured and unsecured

Debentures which create a charge on the assets of the company are called secured debentures

Debentures which don't create a charge on the assets of the company are called secured debentures

ii) Registered and bearer

Registered debentures are those which are duly recorded in the Register of Debenture holders maintained by the company.

Bearer debentures are those which are issued without the names of debenture holders. These can be transferred by mere delivery.

iii) First and second

Debentures that are repaid before other debentures are repaid are called first debentures

Debentures which are repaid after the first debentures are repaid are called second debentures.

iv) Convertible and non-convertible

Convertible debentures are those which can be converted into equity shares after the expiry of a specified period.

Non-convertible debentures are those which cannot be converted into equity shares.

CHAPTER 10

INTERNAL TRADE

Retail trade

Buying goods from wholesalers and selling them in relatively small quantities to consumers is called retail trade. Person engaged in retail trade is called retailer. Retailer is the connecting link between wholesaler and consumer.

Fixed shop retailers

These are retail shops who maintain permanent establishment to sell their merchandise. Therefore, they don't move from place to place to serve their customers.

Types of fixed shop retailers

The fixed shop retailers are classified into TWO based on the size of their operation

A] Small retailers and B] Large retailers

A] Fixed shop small retailers

1. General Stores

These are most commonly found in a local market and residential areas. These shops carry stock of a variety of products required to satisfy the day-to-day needs of the consumers. They help consumers in buying products of daily use like grocery items, soft drinks, toiletry products, stationery and confectionery etc.

2. Speciality shops

These retail stores specialise in the sale of a specific line of products. They are generally located in a central place to attract a large number of customers. Eg: Shops selling children's garments, men's wear, ladies wear, toys and gifts, school uniforms, college books etc.

3. Street Stall Traders

These retailers are commonly found at street crossings or other places where flow of traffic is heavy. They attract floating customers and deal mainly in goods of cheap variety like hosiery products, toys, cigarettes, soft drinks etc.

4. Second Hand Goods Shop

These shops deal in used goods like books, clothes, automobiles, furniture and other household goods etc. Generally persons with low income purchase goods from such shops. The goods are sold lower prices.

B] Fixed shop large retailers

1. Departmental Stores

A departmental store is a large retail store offering a wide variety of products under one roof. It has a number of departments each one dealing in one type of product. For eg: there may be separate departments for toiletries, medicines, furniture, groceries, electronics, clothing etc within one store. "Needle to an aeroplane", "all shopping under one roof", " a pin to an elephant" is the spirit behind a departmental store. Eg: Akberally in Mumbai, Spencers in Chennai etc.

Features

a) A modern departmental store may provide all facilities like restaurant, travel and information bureau, telephone booth, rest rooms etc.

b) These stores are generally located at a central place in the heart of a city.

c) They are generally formed as joint stock companies.

d) They purchase directly from producers and operate separate warehouses.

e) All the purchases in a departmental store are made centrally by the purchase department of the store.

2. Chain Stores or Multiple Shops

Chain stores are networks of retail shops that are owned and operated by manufacturers or intermediaries. Under this type of arrangement, a number of shops with similar appearance are established in localities, spread over different parts of the country. These shops deal in standardised and branded consumer products. Eg: DCM, Raymonds, Bata, KFC etc.

Features

a) These shops are located in populous cities.

b) The production/purchase of merchandise for all the retail units is centralised at the head office.

c) Each retail shop is under the direct supervision of a Branch Manager

d) All the branches are controlled by the head office.

e) The prices of goods in such shops are fixed.

f) All sales are made on cash basis

g) The head office normally appoints inspectors, who are concerned with day-to-day supervision of the shops.

Advantages

i) Elimination of middlemen

By selling directly to the consumers, the multiple shops can eliminate middlemen in the sale of goods and services.

ii) No bad debts

As all the sales are made on cash basis, there are no losses on account of bad debts.

iii) Transfer of goods

The goods not in demand in a particular locality may be transferred to another locality where it is in demand.

iv) Diffusion of risk

The losses incurred by one shop may be covered by profits in other shops.

v) Low cost

Because of centralised purchasing, elimination of middlemen, the multiple shops have lower cost of business.

vi) Flexibility

If a shop is not operating at profit, the management may decide to close it or shift it to some other place.

Limitations

i) Limited selection of goods

multiple shops don't sell products of other manufacturers. So, the consumers get only a limited choice of goods.

ii) Lack of initiative

The persons managing the multiple shops have to obey the instructions received from the head office. This takes away the initiative from them to use their creative skills to satisfy the customers.

iii) Lack of personal touch

Lack of initiative in the employees leads to indifference and lack of personal touch in them.

iv) Difficult to change demand

If the demand for the merchandise changes rapidly, the management may have to sustain huge losses because of large stocks lying unsold at the central depot.

3. Supermarkets

A supermarket is a large retail business unit selling wide variety of consumer goods on the basis of low price, wide variety and self-service. The goods traded are generally food products and consumer products such as grocery, utensils, clothes, electronic appliances, household goods and medicines. The customers move into the store, pick up needed goods, bring them to the cash counter, make payment and take home the delivery.

Features

a) A supermarket generally carries complete line of food and non-food products

b) The buyers can purchase different products as per their requirement under one roof.

c)A supermarket operates on the principle of self-service

d)The prices of the products are lower than other types of retail stores.

e) The goods are sold on cash basis only

f) The supermarkets are located at central locations.

Vending Machines

These are machines operated with coins or cards for the sale of goods and services. Vending machines are used for the sale of hot beverages, platform tickets, milk, soft drinks, chocolates, newspaper etc. The best example is ATM.

Vending machines are useful for selling pre-packed brands of low priced products. But the cost of installation and its regular maintenance is high. Also consumers cannot see the product before buying and don't have the opportunity of returning unwanted goods.