CHAPTER 14

TRADE ASSOCIATIONS AND OTHER ENTERPRISES (II)

Objective

At the end of this chapter the students will be able to identify other forms of enterprises such as cartels, trusts and amalgamations and reasons for their formation.

14.1 Consortium

A consortium is the coming together of independent firms or business units in order to undertake a project. The association of such firms is for the purpose of quoting for, and if successful would undertake to complete such projects. By nature, such projects must have required skills and resources that are not ordinarily possessed by anyone of the firms in the association. Consequently, the driving force behind a consortium is for its members to place at the disposal of the consortium all the resources necessary for the implementation of the contracts or projects the firms have won jointly. By practice, a consortium is temporary and usually for one project or contract only. When such an association becomes permanent, it is then known as a syndicate. For instance, consortium could be formed among firms of structural engineers, civil engineers, architects and quantity surveyors for the purpose of a road construction project.

14.2 Syndicate

A syndicate is an association of organizations or individuals who work together for a common legitimate trade or business interest. For instance, the underwriters at Lloyds (in London) are a syndicate for the purpose of undertaking business in marine insurance. However, there could be syndicates of robbers or smugglers.

Although, syndicates are of more permanent nature than a consortium, all the same, each member of a syndicate retains his independence, but only act in concert in the pursuit of certain common objectives. Other good examples of syndicates are the London Discount Market Association and the Nigeria Discount Houses Association who come together to make weekly tender for treasury bills.

14.3 Cartel (or Kartel)

A cartel is another form of association of business formed for the main purpose of exercising a measure of monopoly, in order to secure higher profits for its members. To this end, a cartel seeks to regulate prices, outputs or market conditions in an industry. Hence, cartels combine only in firms of the same line of industry. Cartels originate from West Germany as Trusts are from the U.S.

Cartels can be national or international. An example of the former was the steel and amenities cartels, headed by Krupp in the 1930s in Germany; while the examples of the latter are the Organization of Petroleum Exporting Countries (OPEC), of which Nigeria is a member, and the International Air Transport Association (I.A.T.A.). Early in 1987, a cartel was formed for African petroleum exporting countries with Nigeria as one on the leading member countries.

The Operation of Cartels

(i) Cartels operate a quota system, whereby every member is asked to produce a certain quantity of membersâ€™ products.

(ii) The pool of membersâ€™ products is put in care of a syndicate for purposes of marketing.

(iii) The syndicate is able to â€˜policeâ€™ the members in order to ensure that the quota allocated is not exceeded by the members.

(iv) The selling syndicate also sees to the distribution of revenue and profits from the sales of â€˜syndicate membersâ€™ products.

(v) Cartels may be for short time only and it is voluntary.

14.4 Trusts

A trust is a group of firms or companies that have combined to reduce competition and control prices to their own benefit or advantage.

Differences between Trusts and Cartels

(i) Trusts would combine different types of industries such as banking, insurance, transport, communication, trade etc. whereas, cartels would combine firms in identical industry only, e.g. organizations producing and exporting petroleum only.

(ii) In a trust, the member organizations do lose their individual economic and legal independence; but in cartels, member firms retain and guide jealously their independence.

(iii) Trusts do combine on very long-term basis while cartels operate on short-term basis.

(iv) In trusts, all the products of members are put in care of trustees for management, marketing and distribution of profits from operation. This is against the employment of syndicates in cartels.

(v) Trusts issue out certificates to members as evidence of individual holdings with the trustees. Cartels make no use of certificates as evidence of individual quotas to the group, but merely keep a record of such individual contributions.

It must be added that, because of the operation of trusts, the trusts have been likened to a monopoly. This is shown in its country of origin, the United States of America, where every

U.S. legislation against monopolies and restrictive trade practices have been regarded as *anti-trust laws.*

14.5 Amalgamations, Combines and Mergers

Amalgamations, combines and mergers are used in respect of the coming together of business organizations in order to achieve some economic objectives. Such a combination or coming together may take different forms. When business organizations combine and the businesses lose their individual identities to form a single concern, then we have *merger,* a complete reorganization or an amalgamation. This type of combination could be permanent. On the other hand, some businesses come together as partial combination only, in which case, each organization still retains its company identity, e.g. syndicate or case, each organization still retains its company identity, e.g. syndicate or consortium - these are explained above. As we have also shown, such combinations could be temporary or short-lived, and for achieving a once-for-all objective only.

Some of the Reasons for Industrial Combinations

(i) **Fear of failure and collapse:** Where weaker business organizations are showing signs of distress, such businesses might opt to combine with stronger ones in order to avoid possible imminent liquidation.

(ii) **Avoidance of unnecessary competition:** When busines organizations have to compete for share of the same market, in order to avoid wastes inherent in competitive advertizing resulting in under-selling and under cutting, such businesses could come together and thereby, form a partial monopoly. Furthermore, any other weaker similar concerns in the market could either join in or quit the market. This is otherwise referred to as achieving marketing economics of sales, Cartels (e.g. OPEC) fall into this category.

(iii) **Marriage of Complimentary Management Talents and Production Technology:** For instance, some businesses have the know-how, but not the capital or the up-to-date machinery. Some have the production technology, but not the distributive and marketing expertise. A combination of such businesses may result in achieving what is *known as technical and financial economies.*

(iv) **For the essence of vertical integration:** Some businesses combine in order to obtain direct supply of raw materials for production purposes - for instance, a publishing company may combine with a printing press, paper manufacturing and ink producing industries. By this, the combi nation may achieve **marketing economies of buying** and this is known as *vertical integration.* This will be treated in this chapter.

(v) **Engagement in other fields of operation:** In other cases combinations arise from the desire of member organizations to engage in other fields of operation. Examples are found in syndicates and in a consortium which come together only to prosecute one or more pro-together mainly to prospect for more natural oil minerals.

(vi) **Specialization:-** The need to employ specialists and to provide welfare and research facilities, can force firms to combine.

14.6 The Holding Company

The holding company is a sort of an industrial combination which materializes when a company has the majority of the nominal share-holding (by acquiring at least over fifty per cent (50%) nominal shares in one or more other companies.)

The holding company is, therefore, referred to as the *parent company* of the subsidiaries. Usually, the holding company and the subsidiary are incorporated separately and each has a distinct legal entity.

The holding company controls the directorship of the subsidiary, by subscribing the majority of the directors on the board of directors and would possibly appoint the managing director of the subsidiary.

By subscribing the majority of the nominal shares, the holding company has a majority voting power on the board and controls the policy of the board. Personnel, especially experts and professionals within both the holding company and the subsidiary can be pooled together for common use, as required within the group.

In addition, other benefits can accrue to the companies as a group. For instance, any tax allowances accruing to a member group which that member can not utilize fully can be passed on to another member of the group who has the capacity to use such tax allowances.

N.B. Tax allowances have the effect of reducing tax liability of companies; and unless companies record some profits, such companies may be unable to utilize their tax allowances fully.

Some example of holding companies in Nigeria are John Holt, United Africa Company (U.A.C.) and Unilever Plc. The Odua Investment Company, owned jointly by the state governments of Oyo, Ondo and Ogun, is another important example of a holding company which subsidiaries among others include Odua Printing Press, Askar Paints Limited, WEMA Bank and National Bank.

The Holding Company of a Subsidiary Company as a Holding Company to the Subsidiary Company of its own Subsidiary

The holding company of a subsidiary company is equally a holding company to a subsidiary of its own subsidiary. For instance, if company **â€˜Aâ€™** is a holding company to a subsidiary company **â€˜Bâ€™**; it follows that company **â€˜Aâ€™** is a holding company to both subsidiary companies **â€˜Aâ€™** is a holding company to both subsidiary companies **â€˜Bâ€™** and **â€˜C.â€™** That is companies **â€˜Bâ€™** and â€˜C are subsidiaries to the holding company **â€˜Aâ€™**.

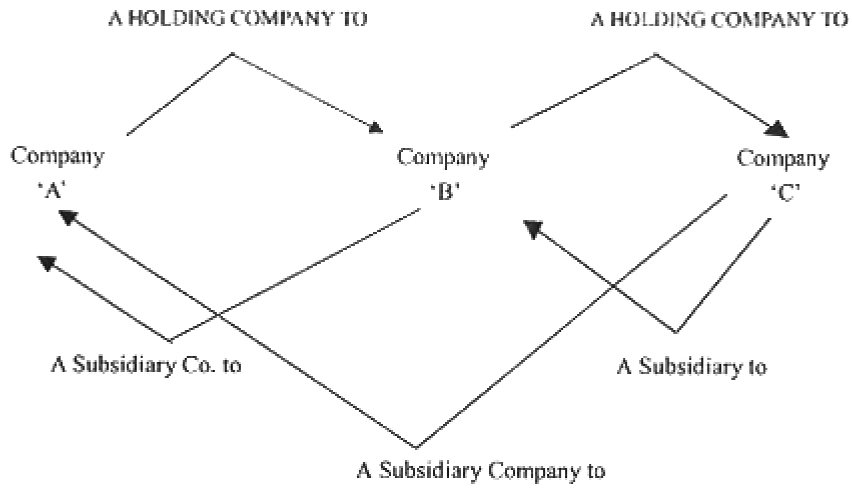

Fig. *13.1:*

N.B. That is, company **â€˜Aâ€™** is a **Parent** company to subsidiary companies **â€˜Bâ€™** and **â€˜Câ€™**.

The Subsidiary Company: It follows from what has been said above, that a subsidiary company is a company in which the majority nominal share capital is held by another company known *as holding or â€˜parentâ€™ company.*

14.7 A Merger

A merger is an amalgamation of two or more firms to form one new company. This must be differentiated from a take-over, i.e. one big company which simply â€˜takes overâ€™ other small ones. In a merger, all the existing companies wind-up and thereby lose their separate legal identities. The assets and liabilities of the defunct member companies in the merger are inherited by the new company.

It is usual to revalue such assets where necessary, in order to ensure that the value attached to such assets are still realistic. In addition, the shareholders in the old firms could, if they wish, exchange their old shares for shares in the new company in an agreed proportion. For these reasons, a merger is alternately known as either a *reconstruction* or an *amalgamation.*

However, while a merger has the advantages implicit in all forms of combinations, like the pooling together or expert personnels and other production resources, a merger might pose some human problems.For instance, it might not be likely that all the existing personnels would be absorbed in the new company, especially if their expertise are not likely to be useful in the new company. The occasion might also be used to retire those who are already due for retirement. Hence, a merger might result in some redundancies. In most countries monopolies commission has to be assured that the merger will not lead to a monopolistic situations. In essence, the objects of a merger are normally to provide and generate greater efficiency.

(i) **Vertical combination:** It is the coming together of various businesses, which hitherto perform different production functions at different levels. The finished products of one might result in raw materials of another; examples are the finished products of ink and paper producing firms, which are passed on to printing press for printing daily newspapers and books. Such combinations must have aimed at connecting up all the stages of production from extraction of raw materials, to convecting them into finished goods, as well as the marketing of such finished goods; thus combining both buying and marketing economics for the members in the vertical combination. Consequently, vertical combination can combine firms in different areas of specialization.

(ii) **Horizontal combination:** This combination, unlike in vertical combination, is for constituent firms that are all engaged in the same line of business, or at the same stage of production. For instance, farmers producing the same type of products - yams, or rice, or cotton, etc. can combine in order to eliminate cut-throat competition in marketing expenses and efforts.

Summary

Consortium: This is a temporary coming together of firms for complementary talent in an effort to make bids for and implementation of projects, e.g. among civil structural engineers and architects and quantity surveyors.

Syndicates: These are individuals or organizations who work together for common legitimate trade interests, e.g. The Lloyds insurance underwriters in London.

Cartels: These are firms in similar business undertakings with units for protection of common interests, e.g. members of OPEC. They operate, e.g. in syndicate for operation of production quotes and uniform price maintenance.

Trusts: A group of firms that have combined to reduce competition.

Merger: Is the fusion together of hitherto independent organizations which come together only to prosecute one or more projects like different oil companies - AP and Total - combining together mainly to prospect more natural oil minerals.

Holding Company: This is a company holding more than 50% shares in other companies, which by that reason would now (the latter companies) be regarded as subsidiaries to the holding or parent company. For instance the ODUA Investment Company is a holding company to a number of subsidiaries such as National Bank, WEMA Bank, Askar. Odua Printing Press Company, etc.

Revision Questions

A. Essay Questions

1. Compare and contrast cartels and trust as forms of business combination.

2. (a) What term is given to firms engaged in the production of different types of manufacturing operations that come together.

   (b) Give two examples of such companies you know?

(c) State 2 things that could be gained from such combinations.

3. What is Consortium?

4. (a) Mention and discuss 5 important reasons why firms come together.

(b) Simply list out 5 different forms by which firms would come together.

(15 mks)

5. (a) Compare and contrast a partnership with a consortium.

(15 mks)

(b) State five professions that by practice engage in partnership.

(5 mks)

B. Objective Questions

1. Another name for amalgamation of business is:
   A. Cartel.
   B. Consortium.
   C. Holding Company.
   D. Merger.
   E. Trust.

NECO (SSCE) 2002

2. Organization of Petroleum Exporting Countries (OPEC) is an example of a/an
   A. Amalgamation.
   B. Cartel.
   C. Consortium.
   D. Holding Company.
   E. Trust.

NECO (SSCE) 2002

3. Where two or more companies agree to work on a project too large for one of them, this is called
   A. Consortium.
   B. Merger.
   C. Combination.
   D. Cartel.

WASSCE 2002

4. A syndicate is an/a
   A. Association formed by the joining together of firms which were previously independent.

B. Association of firms at the same stage of production, formed for the purpose of keeping up prices.
C. Association of firms for the regulation of output and prices.
D. Combination of firms which carry out the same kind of business such as refilling.
E. Company that controls one or more other companies by holding majority of their shares.

NECO (SSCE) 2001

5. An association formed by the joining of firms which were previously independent whereby the old ones completely lose their former individual identities is called
   A. Amalgamation.
   B. Cartel.
   C. Holding Company.
   D. Price ring.
   E. Syndicate.

NECO (SSCE) 2001

6. A voluntary association of independent firms formed for the purpose of executing a large capital project is a
   A. Merger.
   B. Consortium.
   C. Cartel.
   D. Trust.

WASSCE (2000)

7. Which of the following is a function of employersâ€™ association
   A. Undertaking research on behalf of employees.
   B. Promotion of thrift in working.
   C. Promotion of workersâ€™ welfare.
   D. Dissemination of information through sponsored journals.

JAMB (2002)

8. A group of companies is a collection of
   A. Subsidiaries and their holding company.
   B. Firms.
   C. Association and their holding company.
   D. Industries. *JAMB (2002)*

9. The merger of two companies producing the same type of products is an example of
   A. Vertical integration.
   B. Horizontal integration.
   C. Lateral merger.
   D. An acquisition.

JAMB (1995)

10. Which of the following organisation represents those who engage labour in Nigeria

A. Nigerian Labour.
B. Nigerian Employers Consultative Association.
C. Manufacturers Association of Nigeria.
D. Nigerian Union of Local Government Employees.

JAMB (1995)

Project

Make a list of the member countries of OPEC.