Chapter 7

CHAPTER 7 Business Organisations

INTRODUCTION

A business organisation engages in the production, distribution and sales of goods and services for the purpose of making profit. This may be done by an individual, group of individuals or even the government. It may be large or small depending on the capital available. This chapter presents the definition of business enterprise, types of business enterprise, features of business enterprise and advantages and disadvantages of business enterprise.

OBJECTIVES

At the end of this chapter, students should be able to:

- Explain the meaning of a business organisation;
- State the features of business enterprises;
- Explain how each type of business is formed;
- Explain public and private enterprises, by stating their characteristics, advantages and disadvantages;
- Explain sole proprietorship and partnership by stating their characteristics, advantages and disadvantages;
- Explain both the limited liability companies and the cooperative society.

7.1 Definition of a Business Enterprise

A business enterprise is an organisation that is established by either an individual or groups of individuals, government and societies. The aim is to make available goods and services that are readily available to meet the needs of the consumers as and, at when due. Business organizations are set up to make profits. Some of the profits are ploughed back into the business, so that more profits will be realised.

7.2 Types of Business Organisations

7.2.1 Private Enterprise

This is a type of business outfit that is established, financed and controlled by an individual or group of individuals. The main motive of the private enterprise is making of profit. Examples of private business enterprise are sole proprietorship, partnership business, private limited liability company, cooperatives and the joint stock company.

7.2.1.1 Sole Proprietorship

This is also called one-man business. It is easy to set up, and it is owned by one man and in some cases with members of his family. He is therefore responsible for the organisation, financing, coordination and overall control of the activities of the business. Sole proprietorship is found in business activities such as buying and selling, different occupations and even

A Seller/Sole Business Operator

in agricultural activities like poultry, piggery and fishery. The sole proprietor bears the risks of the business alone, while he also reaps the gains all alone.

Characteristics of the sole proprietorship enterprise

(a) Ownership and control: Th e sole proprietorship business is owned and controlled by a single individual. He establishes a business outfit and ensures that the workers perform their tasks under his direction.

(b) Source of capital: Th e capital used in forming and running this business comes from the sole proprietor, his friends, relations, and through credit purchase. In some instances, he can borrow from the bank if he is in good books of such a bank.

(c) Legal status: Th e sole proprietorship business has no legal entity. It cannot sue and cannot be sued.

(d) Motive of formation: It is formed mainly to make profit.

(e) Extent of liability: Th e liability of the sole proprietor is unlimited. If the business fails, the proprietor's belongings can be sold to pay off the debt he owes.

(f) The nature of business: Sole proprietorship business is the oldest, simplest and commonest form of business organisation and it requires small capital.

Advantages of sole proprietorship business

(a) It requires small capital to start such business.
(b) It does not require any rigid and legal formality for its formation.
(c) It is easy to establish.
(d) It guarantees quick decision making.
(e) It is easy to manage due to its small size and its non-complexity.

(f) It guarantees privacy in the business administration.
(g) Th e sole proprietor owns all the profits.
(h) It guarantees closeness and direct contact with the customers.

Disadvantages of sole proprietorship

(a) The sole proprietor bears all the risks.
(b) The business lacks continuity because the death of the proprietor may lead to the end of the business.
(c) The business is not a legal entity. So, it cannot be sued by creditors and cannot sue debtors.
(d) The business faces the problem of inadequate capital.
(e) The business has limited scope of decision and policy making.
(f) The proprietor often works long hours and does not go on leave.

7.2.1.2 Partnership Business

This is a type of business formed by at least 2–20 people, who come together with the aim of maximising profit. Th e owners of this business are called partners.

Characteristics of partnership business

(a) Ownership and control: It is owned and controlled by at least 2 or maximum of 20 people.
(b) Source of capital: Capital is generated from contributions of partners.
(c) Motive of formation: Partnership business is formed with the aim of making profit.
(d) Extent of liability: The liability of partnership business is unlimited except for sleeping or dormant partners.
(e) Legal status: Partnership business is not a legal entity. In essence, it cannot sue and cannot be sued.

Article of partnership / partnership deed: Partnership deed is also called article of partnership and may be defined as the written agreement (usually legal) that governs and guides the partnership business. This deed is usually drawn up by partners or by a legal practitioner and it contains some or all of the following:

(a) The name of the business.
(b) The names of the partners.
(c) The nature of the business to be undertaken.
(d) The amount of capital or resources to be contributed by each partner.
(e) The sharing of profits and losses among partners.
(f) The right of partners in the business.
(g) The method of admitting new partners.
(h) The dissolution of the partnership business.

Types of partners

1. **Ordinary partner**: This partner takes active part in the organization and management of the business. He has unlimited liability.
2. **Sleeping or limited partner**: Th is partner contributes capital but takes no active part in the organisation and the management of the business. He has a limited liability. He receives a fixed rate of interest on his capital without receiving any dividend or additional benefit.

Advantages / merits of partnership business

(a) Talents and skills: There is diversity of talents and skills among the partners, which leads to greater efficiency. For example, a collaboration between an architect, economist, accountant and engineer provides better and more specialized skills in the house construction industry.
(b) Capital: Capital is more easily obtained because of the large number of partners that will contribute money.
(c) Risk-bearing: Burden and risks are shared among the partners.
(d) Decision-making: It guarantees rational, popular, careful and better decision making since many skilled partners come together.
(e) Continuity of business: It guarantees greater continuity since the death of a partner does not lead to the end of the business.
(f) Relationship among partners: Th ere is a close relationship between or among the partners.

Disadvantages / demerits of partnership business

(a) There is delay in decision-making due to the long process of reaching an agreement.
(b) Disputes and arguments may arise among the partners, which could lead to a total dissolution of the business.
(c) It is not a separate entity, and so cannot sue and be sued.
(d) The capital generated is limited by the financial strength of the partners.
(e) There is unlimited liability for ordinary or active partners. If the business fails, the private

assets of the ordinary partners may be sold to off set the business debt.

7.2.1.3 Limited Liability Company

There are two types of limited liability companies and these are as enumerated below.

I. Private limited liability company: This is a company established by 2–50 people who buy shares in the company. By its nature of existence, it cannot offer its shares to the public for subscription.

Characteristics of a private limited liability company

(a) Membership involves a minimum of 2 persons and a maximum of 50 persons.
(b) Its shares are not transferable from one person to another.
(c) Its shares are not offered for public subscription.
(d) It is a legal entity and so it can sue and be sued.
(e) Balance sheet or statement of account cannot be made public.
(f) Shareholders have limited liability. So, in case the business fails, the shareholders will lose only the capital contributed to the business.
(g) Capital is raised through the issue of share to the shareholders.
(h) There is a board of directors that controls the activities of the business.

Advantages / merits of private limited liability company

(a) There is high possibility of raising larger capital since the number of members range from 2 to 50.
(b) The shareholders have limited liability, and if the business fails, the shareholders will lose only their fully paid-up value of their shares.
(c) The business is a separate legal entity. It can sue and can be sued.
(d) The business has greater continuity than the sole proprietorship or partnership. So, the death of a member does not affect the operation and continuity of the business.
(e) The shareholders could leave the control of the business in the hands of the board of directors and use their time profitably in other ventures.
(f) The business enjoys internal economies of scale.

Disadvantages / demerits of private limited liability company

(a) Th e amount of capital raised or generated is not as large as that of public limited liability companies due to the less number of shareholders (2–50).
(b) The shares of the company cannot be transferred from one person to another without proper and formal agreement by the members.
(c) There is delay in decision making, since decisions have to be taken by many shareholders.
(d) The company's shares cannot be advertised for public subscription. There is limited market for subscription of the company's shares.

II. Public limited liability company / Joint stock company: A joint stock company is a form of public limited liability company formed by private individuals and organisations (not government or state owned). Shares of the company are off ered for public subscription and shareholder's liabilities are limited to the capital they contributed. Examples of these companies include University Press PLC, UAC (Nigeria) PLC, Nigerian Bottling Company PLC, Cadbury Nigeria PLC, First Bank Nigeria PLC, etc.

Characteristics of a joint stock company

(a) Membership size ranges from seven to infinity.
(b) The business is a separate legal entity.
(c) The liabilities of the members are limited.
(d) The business has a greater continuity of existence since there are many members and there is a large source of capital.
(e) Capital is generated from members and since membership size has no limit, the sum of capital can be very high.
(f) Shares are transferable from one person to another.
(g) Shares are offered for public subscription.

Advantages / merits of a joint stock company

(a) Shareholders enjoy limited liability. Liability of shareholders is limited to paid-up value of their shares.
(b) The business has possibility of raising large capital due to large membership size.
(c) The business ensures easy transfer of shares from one person to the other.
(d) The business risks and burdens are shared among a large number of people.
(e) The business has a perpetual existence. In essence the death of one member cannot lead to the dissolution of the business.

(f) The business account is made open because there is accountability and transparency.
(g) The company has the ability to secure the service of efficient managers and other skilled personnel because of its large size.
(h) The business has a high degree of specialisation.
(i) The employees could become co-owners of the business by purchasing shares in the company.
(j) The shares subscribed into can be translated to cash through the stock exchange market.

Disadvantages / demerits of a joint stock company

(a) There is no privacy in the operations of the business. In essence, the public company has to publish an audited account yearly for public inspection.
(b) Conflicts of interest may arise between paid managers and shareholders; this conflict may be between the idea of using the company's profit for further investment and the increment of shareholders' interest.
(c) The shareholders in the practical sense do not have control over the business. The business is often controlled by few individuals who are managers of the company.
(d) There is lack of personal contact between the management and employees and between the company and its customers.
(e) There is lack of personal relationship between the management and the shareholders due to the large number of members.
(f) A joint stock company is not easy to set up. Th is is because of the numerous registration requirements by the registrar of companies and the large capital involved.
(g) Th ere is much bureaucracy and protocols in joint stock company, which lead to delay in decision making.
(h) Some decisions are taken without the consent of the shareholders.

Formation of a Company

In the formation of a company, some legal procedures have to be followed before the company is formed. Th is is in accordance with the Nigerian Company's Act 1958. The following stages must be followed:
(a) The business will file a number of documents with the registrar of companies. Such documents include:

- The memorandum of association
- The article of association
- The names of the would-be directors of the company
- An undertaking or declaration that the company has satisfied all the necessary conditions for the company's formation.

(b) The registrar will then send a certificate of incorporation if he is satisfied that the company has met the necessary requirements for its formation.
(c) The company will send a copy of its prospectus to the registrar of companies.
(d) The registrar (after verification) will send a trading certificate.
When all these processes are completed, the business can start functioning as a company. The completion of all these legal procedures help to prevent penalizing of the prospective shareholders under the company's fraudulent act.

Documents involved in the formation of a company

(a) Memorandum of Association: This gives detailed information about the business and its relationship with the outside world. It includes the following:

- The name and address of the business
- The nature of the shareholders' liability
- The types and values of share capital
- The objectives of the company

(b) Article of Association: This document is more or less the constitution of the company. It includes the following:

- Rules and regulations of the company
- Voting rights of shareholders
- The time of meetings
- The procedure for appointments to post or offi ces
- The power of the directors

Sources of finance for small and large private business firms

(a) Self-financing: Business could be financed by the owner or founder of such business.
(b) Buying on credit: Business can be run by getting goods on credit to be paid later or as it

makes sales.
(c) Loan from commercial banks: Small and large firms who are credit worthy could borrow from commercial banks to finance their businesses.
(d) Selling of shares: This is a major way by which large firms raise capital. The public limited company sells shares through a registered company or by itself. The company calls on the public to subscribe to its shares. The company then issues prospectus which contains details about the shares to be sold.
(e) By taking debentures: A debenture is an instrument or a loan certificate for raising a long-term loan from the members of the public by a limited company. A debenture holder receives a fixed interest on his capital and his money is repaid at maturity, even if the business does not make profit.
(f) Borrowing: Borrowing from friends and relatives is common and applicable to the small firms or a sole proprietorship business as a source of financing the business.
(g) Other sources: These include government subsidies, subvention and grants, tax holidays and rebate.

7.2.1.5 Cooperative Societies

This is a form of private business organisation established by people with a common interest in order to protect the interest of its members.
Origin: Cooperative movement started in Rochade, a town in Britain, in 1844. Twenty-eight artisans, called the "Rochdale Pioneers", contributed a few pence per week and obtained an initial capital of £28.00. With this amount, they started a retail shop. Members bought in cheap prices from this shop and profits were distributed
to members in proportion to the amount of business done through the cooperative.

Types of cooperative societies

(a) Consumers' cooperative society: This is organised by consumers who wish to advance their interests in retail purchases. They buy in bulk from manufacturers and sell at affordable prices among themselves.
(b) Producers' cooperative society: This is organised by producers of similar products. They pull their resources together in order to better their welfare.
(c) Thrift and credit cooperative society: This is a loan-giving society where members save or contribute to a common purse and can take about 2–3 times the amount saved as loan at reduced interest rate. The profits realised are shared among members according to their contribution.

Characteristics of cooperative societies

(a) There is no limit to the size of its membership.
(b) The organisation is managed and controlled by the members.
(c) All members have equal voting rights in decision making irrespective of the shares held. Hence, it is democratic in nature.
(d) Members have unlimited liability.
(e) It is set up to help its members who have pooled their financial resources together.
(f) Profits or dividends are shared according to the members' patronage or shares ownership. Th is means the higher the number of shares, the higher the dividend and vice versa.
(g) Initial capital is raised by selling shares to the members.
(h) The business is not a separate legal entity. Hence, it cannot sue and cannot be sued.

Advantages / merits of cooperative societies

(a) It is set up for the common good of its members.
(b) Members are encouraged to be thrifty to cultivate the habit of saving for the rainy days.
(c) It guarantees equal voting rights in the decision-making process to its members irrespective of the amount of shares held.
(d) It provides financial support for members by providing credit facilities.
(e) The business has greater continuity than partnership and sole proprietorship business.
(f) Their profits are exempted from taxation.

Disadvantages / demerits of cooperative societies

(a) Most of the members are illiterates and this may lead to wrong use of their voting rights.
(b) Business funds are often diverted for political use which is not for the benefit of its members.
(c) Credits and loans are given mostly to highly influential people and may not be given to less influential members who need the credit.
(d) It is less competitive with other forms of business enterprises.

7.2.2 Public Enterprises

There are government or state-owned business organisations set up by an "Act of Legislation" with the aim of providing goods and services to the community. Examples of such enterprises are Federal Radio Corporation of Nigeria (FRCN), Th e Nigerian Ports Authority (NPA), Th e Power Holding Corporation of Nigeria (PHCN) and Nigeria Railway Corporation (NRC).

Characteristics of public enterprises

(a) They are owned by the government or state.
(b) They are established by an "Act of Legislation".
(c) Government provides capital for public enterprises through
the taxes paid by members of the public or loans from banks.
(d) They are established to render services to the public by supplying goods and services at affordable and reasonable prices.
(e) The government bears the risks and burden alone if the business fails.
(f) The business is managed and controlled by the board of directors appointed by the government.
(g) Public enterprise is a separate legal entity. Hence, it can sue and can be sued.

Advantages / merits of public enterprises

(a) They provide social services at cheap and affordable prices for the general public. Examples are provision of water, transport and electricity.
(b) They provide basic infrastructural facilities for the public and general community development. Examples are bridges and road networks.
(c) They help to control private monopoly power exercised by the private companies. If goods and services like water and electricity are provided only by private bodies, the prices will be too high.
(d) They can raise loans from commercial banks and other financial institutions at a cheap rate of interest.
(e) They are established to provide services in key industries and sensitive areas of the economy, which a private company may not be buoyant or capable to undertake. Examples are iron and steel production, telecommunication, central banking and mining of minerals.

Disadvantages / demerits of public enterprises

(a) Bureaucracy: There is high degree of bureaucracy in the public enterprises, which is noted with protocol and routine ways of doing things.
(b) Political interference: Political events or activities affect the business operations of a public enterprise.
(c) Appointment of board members: Appointment of members of the board of directors is politically biased because most appointments may not be based on merit.
(d) Misappropriation of fund: Th ere is high possibility of fraud and misappropriation of public funds.
(e) Decision-making: There is delay in decision-making, which may be due to the large size and bureaucratic nature of the enterprise.
(f) Working condition: The working condition in public enterprises is not always attractive and as a result may not guarantee efficiency.

Problems of business enterprises/organisations in Nigeria

(a) Inadequate capital: Many organisations in Nigeria are faced with the problem of inadequate capital. Th is does not encourage full and large-scale operation.
(b) Inefficient administration and management of the business:
Many business enterprises in Nigeria face the problem of inefficient administration and management, because many business managers do not have the required managerial skills to manage businesses.
(c) Inadequate infrastructural facilities: Infrastructures include roads, railways, transport systems, electricity and water supplies. These facilities are not in their good form in Nigeria and in turn affect business activities.
(d) Political instability: When there is political instability, there is disruption of smooth governmental administration, and this affects the smooth operation of business enterprises. The change in government affects some business policies, as well as the operations of some organisations.
(e) Bribery and corruption: Many Nigerian firms are faced with the problem of bribery

and corruption. This could be in the form of corrupt officials, corrupt managers and employees. Sub-standard companies, fake registration by companies and the sale of fake goods or products are additional problems.

(f) Unfavourable economic condition: Nigerian economy is not favourable for most Nigerian firms because of the following: government ban of materials, scarcity of spare parts for machines and plants, poor power supply and poor road network. With these inadequacies and problems, many firms find it difficult to start or grow.

(g) Obsolete techniques: Some firms are still using old techniques in the modern age. They find it very expensive to buy modern equipment and maintain such equipment even if they can acquire it. Obsolete techniques give room to production of sub-standard products.

(h) Poor accountability and transparency: This could be as a result of poor accounting system of the small-scale business, the corruption of The teacher and students should arrange to visit:

(i) sole trading organisations,
(ii) private limited liability companies,
(iii) public limited liability companies, and
(iv) government-owned corporations in their area.

Class Activity

the manager in public enterprises, and so on. When accountability is poor, transparency will not be guaranteed.

(i) Lack of market for domestic products: Most people in Nigeria prefer foreign goods to locally produced goods. As a result, some firms in Nigeria find it difficult to grow because their expectations and operations are pegged down by the poorly patronised domestic market.

Summary

This chapter discussed the following:

- The definition of the term ‘business enterprise’.
- The definition, characteristics and advantages and disadvantages of sole proprietorship.
- The definition, characteristics, deed of partnership, types of partnership and advantages and disadvantages of partnership.
- The definition, characteristics and advantages and disadvantages of a private limited liability company.
- The definition, characteristics and advantages and disadvantages of a joint stock company.
- The definition, types, characteristics and advantages and disadvantages of small and large private business firms.
- Th e definition, characteristics and advantages and disadvantages of public enterprises.

Revision Questions

Objective Questions

1. Which of the following is not a source of finance for a one-man business?
(a) Money lenders   (b) Inheritance
(c) Loans from banks (d) Loans from insurance company
(e) Sales of shares

2. The main objective of production by an entrepreneur is to:
(a) Equate marginal revenue with marginal cost
(b) Provide employment opportunities
(c) Equate total revenue with total cost
(d) Equate average revenue with average cost
(e) Accumulate wealth for the nation

3. Limited liability means that:
(a) The debts of a company can only be paid from its own assets
(b) The debts of a company are paid from business as well as private funds of the owners
(c) A company does not have to pay its debts
(d) The debts of a company must be paid from private funds only
(e) Government cannot tax a company

4. Which of the following is not a source of providing funds for a public limited company in West Africa?
(a) Bank loans (b) Issue of shares
(c) Issue of debentures (d) Ploughing back profits
(e) Sale of bonds
5. In a public company entrepreneurial functions are performed by the:
(a) Workers (b) Shareholders
(c) Creditors (d) Board of directors
(e) Chairman

Essay Questions

1. What functions do wholesalers perform for manufacturers? **(SSCE 1993)**
2. Compare and contrast the private limited company with the public limited company. **(SSCE 1994)**
3. Give five reasons why government participates in business enterprises. **(SSCE 1995)**
4. Explain five sources of finance that are available to a public limited company. **(SSCE 1996)**
(a) Distinguish between a public company and a public corporation.
(b) What are the problems of public corporations in your country? **(SSCE 2005)**

Glossary

Article of association: A document that explains the relationship that exists between an organisation and the members of the public.
Joint stock company: A company that is owned by members of the public through the subscription of shares.
Memorandum of association: Explains about the internal activities and the organisation that exists within an organisation.
Partnership deed: Th is is a legal document that guides the activities of the partners in the partnership business.
Private enterprise: It is a business organisation that is owned, financed, controlled and directed by an individual.
Public enterprise: Th is is a business organisation that is owned, financed and directed by the government.