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Teacher view



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Glossary



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# The big picture

You may be thinking about your options after you finish secondary school. One option might be to study at university. You will need to decide on your course and where you want to study. You might also need to decide whether to attend a public or a private university.

Most countries have both public and private universities. Public universities are often owned by governments and may provide courses with lower tuition fees than private universities. In some countries, such as Germany, Norway and Sweden, tuition fees at public universities are very low, even to international students who qualify for entry. In China, tens of millions of students receive free education, many of whom attend long-established public universities such as Tsinghua University and Nanjing University. In the United States, many public universities are owned by individual states. Examples of these are the University of California at Berkeley and the University of Virginia. These universities often have programs adapted to the needs of the state where they are located and charge lower fees to state residents.



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**Figure 1.** Most countries have both public and private universities.

Credit: Hispanolistic, Getty Images


In the UK, public universities are independent. They are not owned by the government but they do receive some government funding. The rest of their income comes mainly from tuition fees. Examples of public universities include the London School of Economics and the University of St Andrews. The UK has a few private universities, which receive all of their income from tuition fees.

In recent times, the number of private universities has grown in most countries. This has been the case even in countries like China, where the state plays a large role in managing the economy. Most students in India, Malaysia, Japan, South Korea, Indonesia and the Philippines attend private universities. Many of these private universities are non-profit organisations, such as New York University which has campuses in New York, Shanghai and Abu Dhabi. In a non-profit organisation, any money left over after costs have been deducted needs to be reinvested into the institution. Non-profit organisations are also allowed to receive donations, which fund endowments worth billions of dollars. These funds are available to finance world-class facilities and exceptional professors.

Some private universities are for-profit organisations. Unlike non-profit organisations, these universities do not reinvest money back into the university. Instead, the leftover money is distributed among shareholders. While this makes it attractive for private investors to set up institutions (the growth of these types of businesses has been enormous in recent years), the profit objective may change the way the education institution operates and how it produces and distributes value in the organisation.



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In this subtopic, you will explore the different types of business organisations and how their legal status is related to their objectives and operations. This is an exciting area of business management, because of the new ways in which markets, the state and society are working together to serve human needs.



## Activity

**Learner profile:** Inquirers

**Approaches to learning:** Research skills (information literacy)

This subtopic looks at different types of businesses and their characteristics. To help you keep track of all the information, set up a mind map with 'Business entities' in the centre.

As you read, add information to your mind map, organising the different types of businesses on the map in a way that makes sense to you. It is especially easy to develop and edit a mind map with digital tools such as [Miro](https://miro.com/mind-map/) (<https://miro.com/mind-map/>), [MindMeister](https://www.mindmeister.com/) (<https://www.mindmeister.com/>) or [Coggle](https://coggle.it/?r=mms&dpm=39489) (<https://coggle.it/?r=mms&dpm=39489>), or any other that you are familiar with.



## International Mindedness

Regulations and cultures in different countries may affect the legal structure that businesses choose. In some countries, certain types of businesses are more commonly established as public organisations, whereas in other countries they might be established as private organisations, as we have seen with universities.



## Concept

### Creativity and ethics

Creativity in businesses plays an important role in developing new and innovative ideas, and in formulating these ideas into products that people want. Private sector businesses face competition and public sector organisations are accountable to society; both must offer value to succeed.

Business ethics should be an underlying feature for private and public sector businesses. Ethics is the moral conduct of businesses to do the right thing. Some ethical behaviour is coded in laws and regulations. But much ethical behaviour is grounded by the mutual responsibilities that develop between networks of stakeholders — like employees, customers, shareholders and suppliers — when organisations are established. An ethical organisation considers and cares for those in



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its sphere of influence. Aside from being the right thing to do, ethical business practices strengthen the resilience and integrity of a business, helping it endure in the long run.

Both private and public sectors must behave ethically. The role and importance of social value and working ethically within the public and private sectors are seen in equality in hiring, delivering on time and maintaining commitments. The public sector also focuses on the legal and political stance as it is directly responsible to people.

### Learning objectives from the IBDP Business Management guide with assessment objective level:

- **Distinguish** between public and private sector (AO2)
- **Examine** the main features of the following types of organisations: (AO3)
  - sole traders
  - partnerships
  - private traded companies
  - public traded companies
- **Examine** the main features of the following types of for-profit social enterprises: (AO3)
  - private sector companies
  - public sector companies
  - cooperatives
- **Examine** the main features of the following type of non-profit social enterprise: (AO3)
  - non-governmental organisations (NGOs)

1. Introduction to business management / 1.2 Types of business entities

## Distinction between private and public sectors

Private and public sectors Private and public sectors

When learning about an organisation, it is important to consider who the organisation belongs to. A bus company owned by the government, for example, is likely to have different priorities from a bus company owned and run by a private company intending to earn a profit.



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This section will look at the how the priorities of organisations that operate in the private sector and organisations that operate in the public sector are different.



## Register of Public Sector Bodies 2020 - Final



**Figure 1.** The public sector in Ireland.

Credit and copyright: The Government of Ireland (<https://www.cso.ie/en/releasesandpublications/ep/p-rpbi/registerofpublicsectorbodies2020-final/>), CC-BY 4.0 (<http://opendefinition.org/licenses/cc-by/>)

More information for figure 1

The image is a circular diagram representing the different categories within Ireland's public sector as outlined by the Register of Public Sector Bodies 2020. The center of the chart shows a building icon labeled 'Public Sector'. Surrounding this center are eight labeled segments, each representing a category: 1) Central Government Departments, 2) Extra-Budgetary Funds, 3) Additional Votes, 4) Non-Commercial Agencies, 5) Commercial Agencies, 6) Social Security Funds, 7) Local Authorities, and 8) Regional Assemblies. Each segment is depicted with a different icon; for example, the 'Central Government Departments' segment features an icon of a government building, while 'Extra-Budgetary Funds' includes an icon of a money bag. 'Approved Housing Bodies' is also labeled outside the segments. The diagram is designed to illustrate the priorities and structure of public sector organizations.

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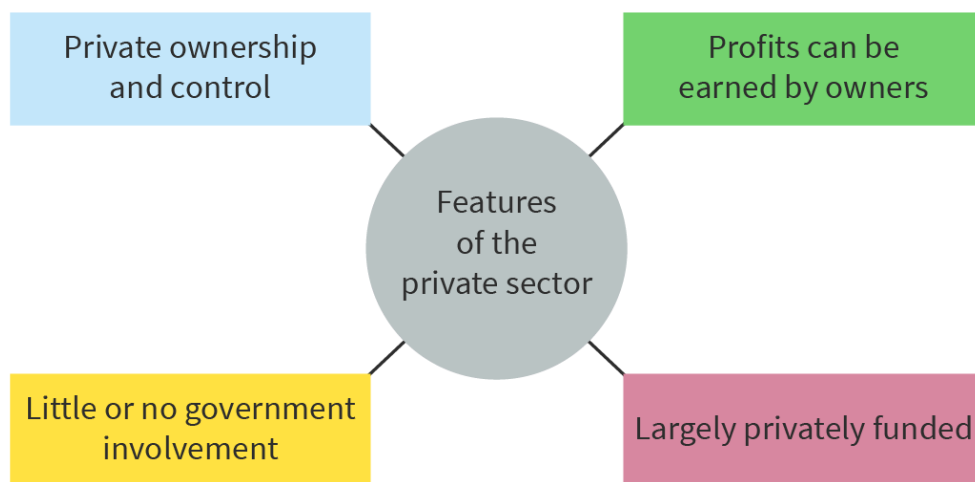
# The private sector

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Businesses in the private sector are owned and controlled by private individuals. Decisions about the business are taken by its owners; the government rarely takes part in decision-making.

Private sector businesses vary in size. They can be small businesses, owned and run by one person, or they can be huge multinational companies operating globally and run by shareholders. Private sector businesses provide many goods and services that people need (such as cars, mobile phones, food or insurance) at a market price. Their business activities provide profit for their owners. However, these goods and services can only be accessed by people who are willing and able to buy these products.



**Figure 2.** Features of the private sector.

More information for figure 2

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The image is a diagram depicting features of the private sector. In the center, there is a circle labeled "Features of the private sector." Four arrows extend outwards from this central circle, each pointing to another circle.

1. The top left circle is labeled "Private ownership and control," indicating that control is generally in the hands of private individuals or groups.
2. The top right circle reads "Profits can be earned by owners," highlighting that profits generated by the business accrue to its owners.
3. The bottom right circle is labeled "Largely privately funded," suggesting that financial resources typically come from private investments.
4. The bottom left circle states "Little or no government involvement," meaning that government involvement in these enterprises is minimal.

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The private sector operates in markets, which is one of the areas of the embedded economy described in [Section 1.1.3 \(/study/app/business-hl/sid-351-cid-762729/book/the-economy-id-36501/\)](#). The private sector and its markets play an important role in the success of any economy by:

- creating employment
- helping the development and growth of the economy
- providing a wide variety of goods and services

The private sector consists of sole traders, partnerships, privately held companies and publicly held companies. You will find out more about these types of businesses in [Section 1.2.2 \(/study/app/business-hl/sid-351-cid-762729/book/forprofit-commercial-enterprises-id-36509/\)](#).



## International Mindedness

Economies around the world have different approaches to the private and public sectors. For example, the USA has a more free-market approach (and less government intervention), has fewer rules and legislation to start businesses, and may rely on the private sector to provide goods and services to residents. This can increase competition, innovation and research and development.

However in other countries, such as China, the government plays a greater role in the managing the economy, providing more goods and services through the public sector.

## The public sector

Public sector organisations are created, owned and controlled by the government. The public sector provides essential goods and services including health care, education and emergency services such as the police and fire services. These services are underprovided by the private sector since they are not profitable to provide, or are unaffordable (inaccessible) to some members in society. The government uses tax revenue to provide these services to the public.

National governments often provide education, health care and protection to their residents through the public sector. National governments are often responsible for defence and transportation infrastructure, including roads, railways and airports. And as you learned in [Section 1.2.0 \(/study/app/business-hl/sid-351-cid-762729/book/the-big-picture-id-36507/\)](#), the

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governments in many countries also own and run universities. Other organisations run by national governments may include museums, hospitals and mail delivery services, as well as embassies, consulates, immigration services and customs offices.

Local governments also provide public services. They often own and run schools, hospitals, police forces and fire departments. Local governments may also be responsible for providing drinking water, for treating wastewater and for recycling or disposing of rubbish.



**Figure 3.** Providing public services.

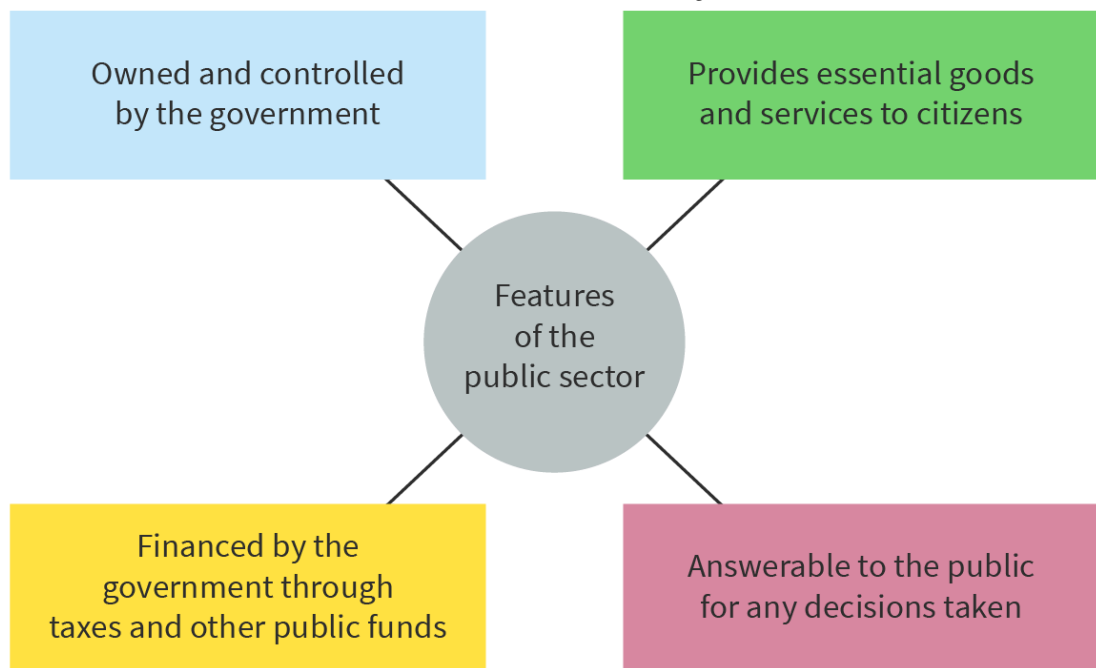
Credit: simonkr, Getty Images

Examples of public sector businesses are the UK's public service broadcaster, the BBC, and the USPS (the United States Postal Service) in the US. Some organisations provide goods and services that are owned and operated by the public sector, such as the Dubai Metro (train) services in the United Arab Emirates (UAE). In this organisation, the costs of operations are funded by the UAE government, but commuters still have to buy a ticket to travel.




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**Figure 4.** Features of the public sector.

 More information for figure 4

The diagram shows a central circle labeled "Features of the public sector." Four boxes surround the circle, each connected by a line. The top left box (light blue) reads, "Owned and controlled by the government." The top right box (green) states, "Provides essential goods and services to citizens." The bottom left box (yellow) indicates, "Financed by the government through taxes and other public funds." The bottom right box (pink) says, "Answerable to the public for any decisions taken." Each box highlights a key feature of public sector organizations.

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To summarise, organisations in the public sector usually have the provision of services to the wider community as their primary objective, funded through taxes. Businesses in the private sector are usually driven by the need to provide goods and services to a more limited group who can pay for them, and they earn profits as a result.

## Theory of Knowledge

Some countries deliver more of their essential social services for human needs like health care through the private sector. Other countries deliver more of these social services through the public sector.

- What assumptions, values and/or beliefs of a population may lead a country to prefer a private or public approach to meeting human needs?



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- To what extent should the public sector collaborate with the private sector for the welfare of the society and the environment?



## Activity

**Learner profile:** Thinkers

**Approaches to learning:** Thinking skills (critical thinking)

Health care, housing, education and infrastructure services such as building highways and street lights are provided both by the public sector and the private sector.

However, the aims of both sectors are different. While both sectors aim to provide goods and services, the private sector earns profits. The public sector provides goods and services, but it is funded through taxation and can serve a wider range of people.

Watch the video below to compare and contrast the aims of the public and private sectors. As you watch, think about these questions:

- How are free education and health care provided by the public sector likely to be different from these services provided by the private sector?
- To what extent is the provision of goods and services for human needs only or mainly the responsibility of the public sector?


- Private Sector vs. Public Sector



**Video 1.** The differences between the private sector and the public sector.



## Case study

In the past ten years, the United Arab Emirates (UAE) has built state-of-the-art infrastructure, health care and education systems. The UAE provides a highly developed health care system through both the private and public sectors, and the level of care is high. In 2018, a [Bloomberg health efficiency survey](#) 



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(<https://gulfnews.com/uae/health/where-does-uae-rank-in-global-health-care-1.2282271>) ranked the UAE in the top 10 most efficient health care systems in the world. Technology-advanced medical facilities are of excellent quality. While UAE citizens receive free health care in the public system, expatriates (people from abroad working in the UAE) usually receive care in the private sector, where English is commonly spoken and many of the medical professionals have been trained in other countries.

### Questions

1. Distinguish between the private sector and the public sector. [4 marks]
2. Explain why health care provided by the private sector might be more expensive than that provided by the public sector in the UAE. [2 marks]

#### Question 1

Private sector organisations charge a price for their products. Their products can only be accessed by those who are willing and able to pay the price. This enables private sector businesses to earn a profit. The case study points out that expatriates in the UAE usually access private health care services.

Public sector organisations are run and operated by the government. Their services are often free of charge or delivered at very low fees. In contrast to the private sector, the public sector usually provides a service to the general public. Public sector businesses aim to provide basic goods and services to society and are usually funded through tax revenues. The case study points out that citizens are offered free health care in the public sector in the UAE.

**Distinguish** between is an AO2 level command term requiring that you make clear the differences between two or more concepts or items.

- Both the private and public sectors need to be described and a contrast clearly highlighted. You should write visibly separate, short paragraphs, each describing a sector (theory) and using information from the case study (example) to support the response.
- Other responses are possible and would be rewarded if appropriate.
- To achieve full marks, you must always include theory and application to the case study in your responses.

#### Question 2

Health care provided by the private sector is provided for a price and is offered by private businesses who aim to make a profit. The private sector may provide greater choice and quality, and the price of medical care may be higher because the costs of offering care are also likely to be higher. The case study points out that expatriates, who may have higher salaries or care financed by employers in other countries, access private health care in the UAE.

**Explain** is an AO2 level command term requiring a detailed account including reasons or causes. Explain why, explain how.



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- Only one point needs to be made.
- Other responses are possible and would be rewarded if appropriate.
- To achieve full marks, you must always include theory and application to the case study in your responses.

## 3 section questions ^

### Question 1

Which sector includes businesses that aim to make a profit?

The private sector



### Accepted answers

The private sector, private-sector, private sector , Private sector, private Sector, Private, private

### Also accepted

sector privado, El sector privado, privado, Privado, Sector privado, Private sectors, Sector Privado, A private sector is the one that aims to make a profit., Privada, privadas

### Explanation

The private sector includes all those organisations that are owned by individuals or groups of individuals. Organisations in the private sector usually aim to earn profits for owners for the investment they have made in the organisation.

### Question 2

The  public ☒ sector provides essential services paid for by national and local governments, usually funded through taxes.

### Accepted answers and explanation

#1 public

Public

### General explanation



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The public sector includes all those organisations that are owned and operated by either the central government or local governments (municipalities), or their agencies, such as the National Health Service in the UK.

### Question 3

Which of the following is **not** a feature of the public sector?

- 1 Earning profits
- 2 Financed by the government
- 3 Providing essential services to the public, often free or for very low fees
- 4 Funded by tax revenues



### Explanation

The public sector does not function under a profit-making requirement. These organisations are generally created by governments in order to provide essential goods and services, usually funded through tax revenues.

1. Introduction to business management / 1.2 Types of business entities

## For-profit commercial enterprises

Types of organisations   Types of organisations

The images below show two famous entrepreneurs. Do you recognise them? Jeff Bezos is the founder of Amazon, an online retailer. Cher Wang, an entrepreneur and philanthropist, is the co-founder and chairperson of HTC Corporation and integrated chipset maker, VIA Technologies. An innovator in touch and wireless hand-held devices, she is considered one of the most successful women in computer technology.



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**Figure 1.** Jeff Bezos, the founder of Amazon, a global online retailer.

Source: Seattle City Council (<https://www.flickr.com/photos/seattlecitycouncil/39074799225/>), CC BY 2.0  
(<https://creativecommons.org/licenses/by/2.0/>), via Flickr



**Figure 2.** Cher Wang, entrepreneur and philanthropist.

Source: Robert Scoble from Half Moon Bay, USA

([https://commons.wikimedia.org/wiki/File:Cher\\_Wang\\_in\\_WEF.jpg](https://commons.wikimedia.org/wiki/File:Cher_Wang_in_WEF.jpg)).

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As you learned in Subtopic 1.1 (</study/app/business-hl/sid-351-cid-762729/book/the-big-picture-id-36497/>), starting a business and becoming an entrepreneur is not an easy process. There are financial and external risks and constraints. Many entrepreneurs who start businesses want to earn profits in return for their risks and efforts. Thus, many business owners choose to operate as a for-profit commercial enterprise. These businesses earn profits and distribute them to the owners of the business, which may be one person or thousands of people, depending on the ownership structure. In this subtopic, you will learn about the four main types of ownership structure in the context of for-profit commercial activity:

- sole traders
- partnerships
- for-profit privately held companies
- for-profit publicly held companies

## Sole traders

A sole trader is an individual who owns and runs a business alone. There is little legal distinction between the individual and their business, and this form of organisation is fairly easy to set up. Another advantage of this type of ownership is that sole traders are able to run the business as they see fit and keep all the profits. They can choose whether to reinvest profits in the business, or use them to meet their own financial needs.



**Figure 3.** A small business.

Credit: Howard Pugh (Marais), Getty Images



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Examples of sole trader businesses include people who are self-employed, restaurant owners, freelance workers, fashion designers, tailors and interior decorators. Sole traders can work alone or can employ people to work for them. Often, these are small family businesses started with little capital investment. Personal savings are often used to start this type of business.

In a sole trader business, the success or failure of the business is the responsibility of the sole trader. They are responsible for debts they take on and any losses they suffer. If the business is unable to pay its debts, creditors (such as suppliers and banks, for example) can seize the owner's personal possessions, including their home. Sole traders may hire employees to help them, but these employees have no ownership interest in the business.

Another potential disadvantage of operating as a sole trader is the lack of distinction between the owner and the business. If the owner dies or is unable to work, for example, the future of the business itself may be uncertain. The business of a sole trader, in this case, may end operations, since the business does not have a separate legal identity from the owner. Sole trader businesses cannot be inherited and continued. They need to be unregistered in the event of the owner's death.

Some well-known companies operating currently were started as sole trader businesses. The luxury fashion house Chanel was started by Coco Chanel in 1910 and has become one of the most famous global brands today.



**Figure 4.** Coco Chanel, the founder of Chanel.

Source: in the public domain ([https://en.wikipedia.org/wiki/File:Coco\\_Chanel,\\_1920.jpg](https://en.wikipedia.org/wiki/File:Coco_Chanel,_1920.jpg)), via Wikipedia



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**Table 1. Advantages and disadvantages of a sole trader.**

Advantages	Disadvantages
<b>Easy to set up.</b> There are few legal formalities, regulations and paperwork.	<b>Unlimited liability.</b> The sole trader is legally responsible for the debts of the business. They may have to give up personal assets such as their own property to settle debts.
<b>Profits.</b> All profits go to the sole trader as the owner of the business.	<b>Difficult to finance.</b> Many sole traders have to use personal savings to finance the business. Expansion and growth of the business might be slower.
<b>Fast decision-making.</b> Sole traders do not need to consult with other owners.	<b>High risk of failure.</b> The business may face strong competition from larger, better funded businesses.
<b>Personal service.</b> The small size of the business can help the sole trader to cater to individual customer needs.	<b>High workload.</b> The sole trader must manage their own accounts, human resources and marketing.
<b>Financial records remain private.</b>	<b>Lack of continuity.</b> If the sole trader dies, the business is likely to cease trading.
<b>Section</b>	<b>Possible higher taxes.</b> The owner may have to pay income tax, often higher rates, instead of corporate tax.

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## Partnerships

A partnership involves the creation of a business by two or more individuals, or partners. Partnerships are governed by partnership agreements, which define the ownership interests of the different partners, as well as how major decisions will be made by the partnership. Two partners may set up a business where ownership and control are split equally between the partners, or they may determine another arrangement that suits the purposes of the business. Some common examples of partnership are medical practices and law firms.

A partnership agreement will likely include the following:

- the amount of money put in by each partner
- the sharing of profits and losses by each partner
- the roles and responsibilities of each partner



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- the rules around accepting new partners or withdrawal of existing partners
- the procedures for ending the partnership



**Figure 5.** Medical practices may be set up as partnerships.

Credit: Cecilie\_Arcurs, Getty Images

**Table 2.** Advantages and disadvantages of partnerships.

Advantages	Disadvantages
<b>Easy to set up.</b> There are few legal formalities or regulations to set up a partnership of two or more partners.	<b>Unlimited liability.</b> Partners are legally responsible for all debts if the business fails. They may have to give up their own personal property to settle debts.
<b>Greater access to finance.</b> There is more than one person (partner) to invest in the business.	<b>Lengthier decision-making and potential for disagreement.</b> Partners have to consult each other, so decision-making about the business may take time, and partners may disagree.
<b>Greater efficiency and productivity.</b> As partners specialise in different skills, <b>productivity</b> increases and helps reduce costs.	<b>Legal and financial responsibility.</b> Mistakes made by one partner can reduce profits for all partners.
<b>Financial records remain private.</b>	<b>Lack of continuity.</b> If one partner dies, the deed of partnership (legal agreement) becomes invalid and will have to be made again (depending on laws of the country).



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## Activity

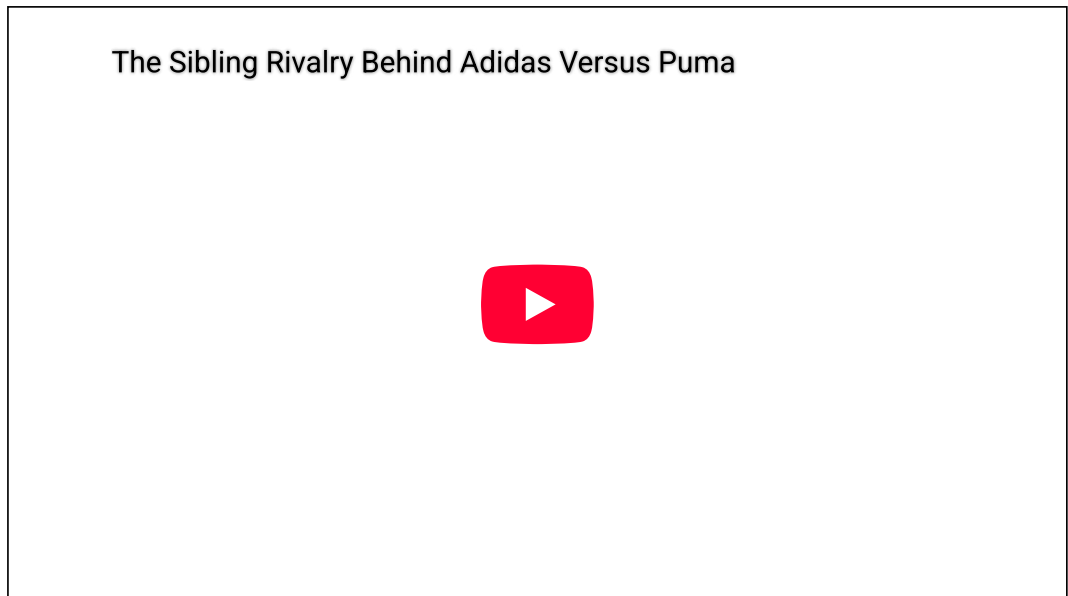
**Learner profile:** Thinkers

**Approaches to learning:** Thinking skills (transfer)

Did you know that the founders of footwear companies Puma and Adidas were siblings?

Puma and Adidas are two of the best-known shoe brands globally. The siblings (brothers Adi and Rudi Dassler) were originally partners in a shoe company "Gebrüder Dassler Schuhfabrik" (English: Dassler Brothers Shoe Factory). The company was started by Adi Dassler, and his brother Rudi joined in 1924. However, after a disagreement following World War II, the brothers went their separate ways and started their own companies in 1948. The following video explains what happened.

What does this story tell you about the potential disadvantages of partnerships?



**Video 1.** The story of the Dassler brothers and how the Puma and Adidas brands were founded.

## Companies (corporations)

A company (corporation) is generally a larger organisation than either a sole trader business or a partnership and is usually owned by many individuals, or groups of individuals, known as shareholders. The term shareholders can be taken literally, as these individuals each own a share of the business. The possession of a single share gives the shareholder the right to:

- vote at the Annual General Meeting, where decisions may be made regarding the management of the company



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- receive a part of the company's profits in the form of dividends if these are paid (however not all companies pay dividends every year)

When businesses are incorporated, they become legal entities separate from their shareholders. These shareholders enjoy limited liability. This means that if the corporation incurs losses, its owners cannot lose more than the funds that they invested in the business. There is a complete separation between shareholders' personal assets and their ownership interest in the business. Even if the company goes into bankruptcy, creditors can only seize the assets of the corporation itself, not the personal possessions of its owners.

Limited liability is a powerful tool that allows companies to access finances more easily than is possible for sole traders and partnerships. Investors can buy shares of the company in the hope of making a good return on their investment without exposing themselves to undue risk. The death of a shareholder has no impact on the continued functioning of the company. Shareholders are, in most cases, also free to sell their shares in the company, and this sale will generally have a limited impact on the company.

Companies whose shares are traded on the stock exchange (where shares may be bought and sold) have to follow complicated regulations. Regulations protect investors who buy shares in a company, but who do not run or control its operations. A board of directors is elected to run the company on behalf of the shareholders. The board of directors represents the shareholders and provides broad oversight of the company's operations.

There are two types of limited liability companies (corporations):

- privately held companies
- publicly held companies

## International Mindedness

Here there is a difference between British and US terminology, with the IB Business Management guide reflecting British usage. In British terminology, 'company' and 'corporation' can be used interchangeably, with both words used only for organisations with shareholders who benefit from limited liability. In the US, however, 'company' is a generic word for a business, and includes sole traders and partnerships as well as corporations.



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## Privately held companies

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A privately held company is privately owned and often has family or friends as the shareholders. The shares are not sold to the wider public and are not traded on a stock exchange. Financial capital is raised from family and friends who then own a share of the company. Shares generally cannot be sold to anyone else outside, without prior approval from all shareholders. This is so that the shareholders retain the ability to make decisions about the company.

Shareholders enjoy limited liability. If the business fails or suffers losses, the personal assets of the shareholders are not at risk. They only suffer losses equal to the value of their shares (the money they have invested in the business).



**Figure 6.** IKEA is an example of a privately held company.

Source: Tiia Monto ([https://commons.wikimedia.org/wiki/File:Kuopio\\_Ikea.jpg](https://commons.wikimedia.org/wiki/File:Kuopio_Ikea.jpg)), CC BY-SA 3.0 (<https://creativecommons.org/licenses/by-sa/3.0/>), via Wikimedia Commons

Two documents are required before privately held companies can start operating. These documents are:

- the Memorandum of Association, which states the details of the company
- the Articles of Association, which states the internal roles and responsibilities of the board of directors and shareholders

Below are some well-known privately held companies.



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- Koch Industries (consumer goods, USA)



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- Deloitte (accounting, UK)
- Visy Industries (packaging, Australia)
- Vodacom Group Ltd (communications, South Africa)
- KPMG (accounting, UK/Netherlands)
- IKEA (furniture, Netherlands/formerly Sweden)
- LEGO (toys, Denmark)
- Huawei (telecommunications, China)
- Tata Group (automobiles, India)
- Lifestyle International (consumer goods, UAE)

**Table 3.** Advantages and disadvantages of privately held companies.

Advantages	Disadvantages
<b>Control and ownership.</b> Control and ownership is shared between a small group of people, usually family and friends.	<b>Profits.</b> Profits are shared between several shareholders.
<b>Greater access to finances.</b> Multiple people can invest in the business. There may be better access to external sources of finance.	<b>Lengthier decision-making.</b> All shareholders need to discuss and agree on decisions.
<b>Limited liability.</b> The personal assets of shareholders are not at risk if the business fails.	<b>Shares cannot be traded publicly to raise finances.</b>
<b>Financial records.</b> These are private and are not made public, enabling the company to take a longer-term view on the development of the company.	<b>Privacy.</b> The business may not be examined by external experts.
	<b>Expensive.</b> It is more costly and time-consuming to set up a privately held company.

## Publicly held companies

Privately held companies that wish to access large amounts of financial capital in order to grow may decide to 'go public' in an initial public offering (IPO). This is where the company sells all or part of the business to external shareholders for the first time. The initial public offering results in the company becoming a publicly held company (public limited company). As owners of the business, shareholders usually receive a portion of the profits earned, or a



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dividend. With a larger number of shareholders, it means that profits of publicly held companies are spread among many more people than is typically the case with privately held companies.

One consequence of becoming a publicly held company is that a business must publish its financial accounts to the public, including its competitors. Another consequence is that it can be taken over by other companies who purchase large quantities of shares.

A publicly held company has a separate legal identity, so it has limited liability for shareholders. The death of one shareholder does not affect the working of the company. Rules and regulations are set up for its formation, working and management. There is no limit on the number of shareholders a publicly held company can have. And there is no legal obligation to inform or obtain consent from shareholders if members want to sell or transfer their shares.



**Figure 7.** Apple is one of the largest publicly held companies.

Source: Arne Müsele (<http://www.arne-mueseler.com/>), CC BY-SA 3.0

(<https://creativecommons.org/licenses/by-sa/3.0/de/deed.en>), via Wikimedia Commons

([https://commons.wikimedia.org/wiki/File:Apple\\_park\\_cupertino\\_2019.jpg](https://commons.wikimedia.org/wiki/File:Apple_park_cupertino_2019.jpg))

Before a publicly held company can start operating, the following two documents need to be in place:

- a **memorandum of association**, which states the details of the company
- **articles of association**, outlining the internal roles and responsibilities of the board of directors and shareholders



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Once the above documents are ready and an application fee is paid, a 'certificate of incorporation' is issued to the company. This is a licence recognising the company as a separate legal entity and allowing it to trade.

Shareholders of publicly held companies meet yearly at an Annual General Meeting to vote for or elect the board of directors and learn about the performance of the business from the chief operating officer. The financial accounts are also presented at the meeting to evaluate the performance of the financial year.

Below are some well-known publicly held companies.

- ICBC (banking, China)
- Apple (computer software and hardware, USA)
- AstraZeneca (pharmaceuticals, UK)
- Airbus (aerospace and defence, Netherlands)
- Saudi Aramco (oil, Saudi Arabia)
- Natura & Co. (personal care and cosmetics, Brazil)
- Adaro Energy (coal mining, Indonesia)
- Reliance Industries (conglomerate, India)
- Sonic Healthcare (health care, Australia)
- Samsung (electronics, South Korea)

**Table 4.** Advantages and disadvantages of publicly held companies.

Advantages	Disadvantages
<b>Finances.</b> Money (capital) can be raised through selling of shares to the public.	<b>Shared profits.</b> Profits are shared between many shareholders.
<b>Risks.</b> The risks are shared among a large number of shareholders.	<b>High costs.</b> It is expensive and a time-consuming process to set up a publicly held company.
<b>Separate legal identity.</b> If one shareholder dies, the business continues to operate.	<b>Loss of control.</b> Outsiders can get control of the business by becoming the largest shareholder.
<b>Limited liability.</b> If the business fails or suffers losses, the personal assets of shareholders are not at risk.	<b>Accounts are publicly available to be viewed.</b>



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## Case study

Mars Inc. is a privately held company in the United States, producing pet food, pet care and food products such as M&Ms, the Dolmio brand and more. With close to 40 billion USD in annual sales, it is one of the largest privately held companies in the world, owned entirely by the Mars family.

Mars is committed to being a privately held company and has no plans to become a publicly held company. The company is famous for its secrecy. Its former chairman, Steven Badger, says that remaining a privately held company allows Mars more freedom to pursue its business activities in the way it wants, enabling it to take a long-term perspective.

Thinking and acting for the long-term health of a business is often not possible in publicly held businesses that have to report earnings to shareholders every quarter. Mars has the advantage of being able to see the actions and earnings of their publicly held competitors, without revealing their own information to the public. This can give the company a strategic advantage. It may also be possible for Mars to reach decisions more quickly than would be the case if there were more shareholders.

### Questions

1. Define the term privately held company. [2 marks]
2. Explain one advantage and one disadvantage for Mars Inc. as a privately held company, instead of a publicly held company. [4 marks]

#### Question 1

Privately held companies are those in which the shares of the company are held by private individuals, often family or friends. The shares are not sold publicly or traded on a stock exchange.

**Define** is an AO1 level command term requiring a precise meaning of a word.

- One mark for a vague definition.
- Two marks for a complete definition.

Definitions do not require application to the stimulus material.

#### Question 2

Advantages:

- Shares are limited to a small group, often family or friends.
- Profits are spread among a smaller group of shareholders.
- Decision-making is often faster.
- Finances remain private and cannot be examined by competitors.
- It is possible to take a long-term view of the business because the company does not have to report quarterly to shareholders.



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### Disadvantages:

- The company has limited access to finance. However, given the size and success of the company, this does not seem to be an issue in this case.
- The lack of scrutiny of finances and actions from outside the company may limit feedback and hinder the development of the company.

**Explain** is an AO2 level command term requiring a detailed account including reasons or causes. Explain why, explain how.

- Only one advantage and disadvantage need to be explained.
- Other responses are possible and would be rewarded if appropriate.
- To achieve full marks, you must always include theory and application to the case study in your responses to the 'explain' command term.

## 3 section questions ^

### Question 1

Which of the following is **not** one of the four main types of legal structure for businesses?

1 Patent



2 Sole trader

3 Privately held company

4 Publicly held company

### Explanation

The four types of for-profit organisations are sole traders, partnerships, publicly and privately held companies. Patents are legal protection for innovation.

### Question 2



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1 Limited liability ✓ (two words) means that if a company performs badly and incurs losses, its owners cannot lose more than the funds that they invested in the business.



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**Accepted answers and explanation****#1 Limited liability****General explanation**

When businesses are incorporated, they become legal entities separate from their shareholders. These shareholders enjoy limited liability. This means that if the company performs badly and incurs losses, its owners cannot lose more than the funds that they invested in the business. There is a complete separation between shareholders' personal assets and their ownership interest in the business.

**Question 3**

What is the name of the process in which all or part of a business is offered for sale to the general public for the first time?

1 Initial public offering



2 Limited liability

3 Legal entity

4 Litigation

**Explanation**

An initial public offering (IPO) is the process where the business offers for sale all or part of the business to the general public for the first time.

1. Introduction to business management / 1.2 Types of business entities

# For-profit social enterprises

For-profit social enterprises For-profit social enterprises

For-profit businesses of all types realise that their business objectives now need to focus more on social and environmental sustainability, while still earning the revenues and profits that ensure economic sustainability. You will learn more about these business objectives in **Subtopic 1.3** (</study/app/business-hl/sid-351-cid-762729/book/the-big-picture-id-36515/>).

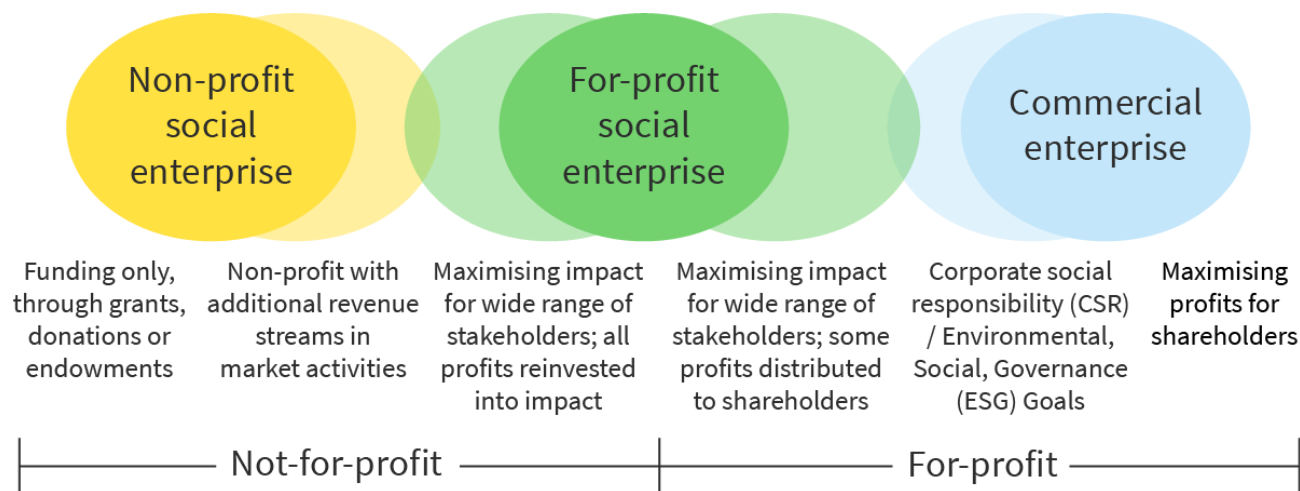


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In the meantime, it can be helpful to think about where businesses stand in the process of moving towards greater social and environmental responsibility by using a continuum, as shown in **Figure 1**.



**Figure 1.** Businesses can be positioned along a continuum.

More information for figure 1

The diagram illustrates a continuum of business types from non-profit to for-profit enterprises. It is divided into three overlapping sections, each represented by a different color and descriptive text. On the left, in yellow, is the "Non-profit social enterprise" section, focusing on funding through grants, donations, or endowments. This section transitions into non-profits with additional revenue streams in market activities.

The middle section, in green, represents "For-profit social enterprises," which aim to maximize impact for a wide range of stakeholders. All profits in one subtype are reinvested into impact, while another subtype distributes some profits to shareholders.

On the right, in blue, is the "Commercial enterprise" segment that includes businesses with a primary focus on maximizing profits for shareholders. These enterprises may also engage in corporate social responsibility (CSR) activities or pursue Environmental, Social, and Governance (ESG) goals.

The continuum is labeled at the bottom as "Not-for-profit" on the left, transitioning to "For-profit" on the right, illustrating the gradual shift from social to financial objectives.

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Some businesses are already highly focused on social and environmental objectives and have been given the label social enterprise. A social enterprise is any organisation that has a social and environmental purpose at its core; it describes the primary purpose of a business, not its legal form. Social enterprises are hybrid organisations that combine the best of the private and public sectors. They are sometimes referred to as a third sector. The term 'social' enterprise is a little misleading as many enterprises are also focused on environmental issues, and even those focused on social issues must work to meet human needs within planetary boundaries.

## Main features of for-profit social enterprises

A for-profit social enterprise is a revenue and profit-making business, but it integrates social and/or environmental impact directly into its business model. It combines the efficiencies, innovation and financial resources that can come from for-profit businesses with the vision and values of social enterprises. Just like for-profit commercial enterprises, these social enterprises can come in the form of sole traders, partnerships, privately held companies or publicly held companies.

The profits of a for-profit social enterprise may be large or small, depending on the strength of demand for its products and how the business is organised. If the social enterprise is offering a good or service at a very low price to consumers in order to increase access, then profits may be low but its impact may be very high. If the social enterprise is paying above average wages, working to regenerate nature through its operations or exceeding other social responsibilities, its production costs could be higher, which could again reduce profits.


Unlike many for-profit commercial enterprises, for-profit social enterprises are judged less on their profits and more on their multi-stakeholder impact. In other words, they are judged on how they are distributing the value that the business generates. Most profits earned are reinvested in the business, to expand its positive impacts and distribute value further. Some profits, however, may also be distributed to the owners of the business, as with for-profit commercial enterprises.



### Activity

**Learner profile:** Inquirers

**Approaches to learning:** Research skills (information literacy), Thinking skills (transfer)

N'Go  (<https://ngo-shoes.com/en/>) Shoes, which produces ethical sneakers in Vietnam, is an example of a for-profit social enterprise.



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Explore the N'Go website [\(https://ngo-shoes.com/en/\)](https://ngo-shoes.com/en/) and watch the video below about the craftswomen who make part of the sneaker. Then answer the following questions:

1. For-profit social enterprises explicitly consider social and environmental sustainability in their business models. Which human needs (social sustainability) are being supported by N'Go? You may want to consider the inner ring of the Doughnut Economics Model from Section 1.1.2 (/study/app/business-hl/sid-351-cid-762729/book/the-doughnut-economics-model-id-36500/) or the social SDGs.
2. How is N'Go meeting its business responsibilities on environmental sustainability? To be specific, you may want to consider the planetary boundaries on the outer ring of the Doughnut Economics Model from Section 1.1.2 (/study/app/business-hl/sid-351-cid-762729/book/the-doughnut-economics-model-id-36500/).
3. For-profit social enterprises, even those that have B Corporation certification (explained below) like N'Go, are not perfect. Look at the report that N'Go wrote about its carbon footprint  [\(https://ngo-shoes.com/\(EN\)%20VDEF%20Impact%20carbone.pdf\)](https://ngo-shoes.com/(EN)%20VDEF%20Impact%20carbone.pdf). How is the company planning to reduce its environmental impact even further in the future?

Meet up in Vietnam with our craftspeople - N'go




**Video 1.** N'Go Shoes is an example of a for-profit commercial enterprise.

In some countries, there are relatively new legal structures relating to for-profit social enterprises, which may set out how profits are distributed within the organisation. The Community Interest Company (CIC)  [\(https://www.gov.uk/government/organisations/office-of-the-regulator-of-community-interest-companies\)](https://www.gov.uk/government/organisations/office-of-the-regulator-of-community-interest-companies) in the UK and Entreprises à Mission  [\(https://www.entreprisesamission.org/\)](https://www.entreprisesamission.org/) in France are examples. There are also certification schemes that can help for-profit businesses improve their credibility in the eyes of consumers



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and investors. The highest profile of these certification schemes is the  
(<https://www.bcorporation.net/en-us>) B Corporation  (<https://www.bcorporation.net/en-us>)  
certification.



## Activity

**Learner profile:** Inquirers

**Approaches to learning:** Research skills (information literacy)

Access the [B Corporation website search page](https://www.bcorporation.net/en-us/find-a-b-corp)  (<https://www.bcorporation.net/en-us/find-a-b-corp>) and find an example of a for-profit social enterprise from your own country.

1. Describe the business. What good or service does it make?
2. Explain how the business is meeting social and/or environmental objectives.
3. Research whether there is a legal structure or certification programme specific to your country for for-profit social enterprises.

## Types of for-profit social enterprises

There are three types of for-profit social enterprises: private sector enterprises, public sector enterprises and cooperatives.

### Private sector for-profit social enterprises

A private sector for-profit social enterprise produces goods and services that are typically sold in markets for a price by for-profit businesses. Many for-profit social enterprises operate in the private sector, meeting many and varied human needs. N'Go, the footwear business in the activity above, is an example. Another example is [Aravind Eye Care](https://aravind.org/) (<https://aravind.org/>) hospitals together with Aurolab (manufacturer of equipment and materials) in India. Its mission is to provide affordable eye care services to people in need, for example affordable cataract surgeries.

### Public sector for-profit social enterprises

A public sector for-profit social enterprise produces goods and services that are typically provided by the public sector. These social enterprises bid for contracts with regional or local governments, who outsource some essential services to for-profit businesses. An example of this is when a local municipality contracts a private firm to carry out recycling services. In some areas, governments contract out ambulance services to for-profit social enterprises.



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By making such arrangements with for-profit companies, governments may be able to lower their costs and focus on other areas of public services. For their part, the businesses can look forward to consistent demand for the essential services they provide. However, governments must maintain some oversight to ensure that the service is being carried out as expected, and they must ensure that if the business runs into financial trouble, the public will not lose access to the service.



**Figure 2.** Some services that were traditionally supplied by the public sector are now supplied by for-profit social enterprises.

Credit: Pramote Polyamate, Getty Images

## Cooperatives

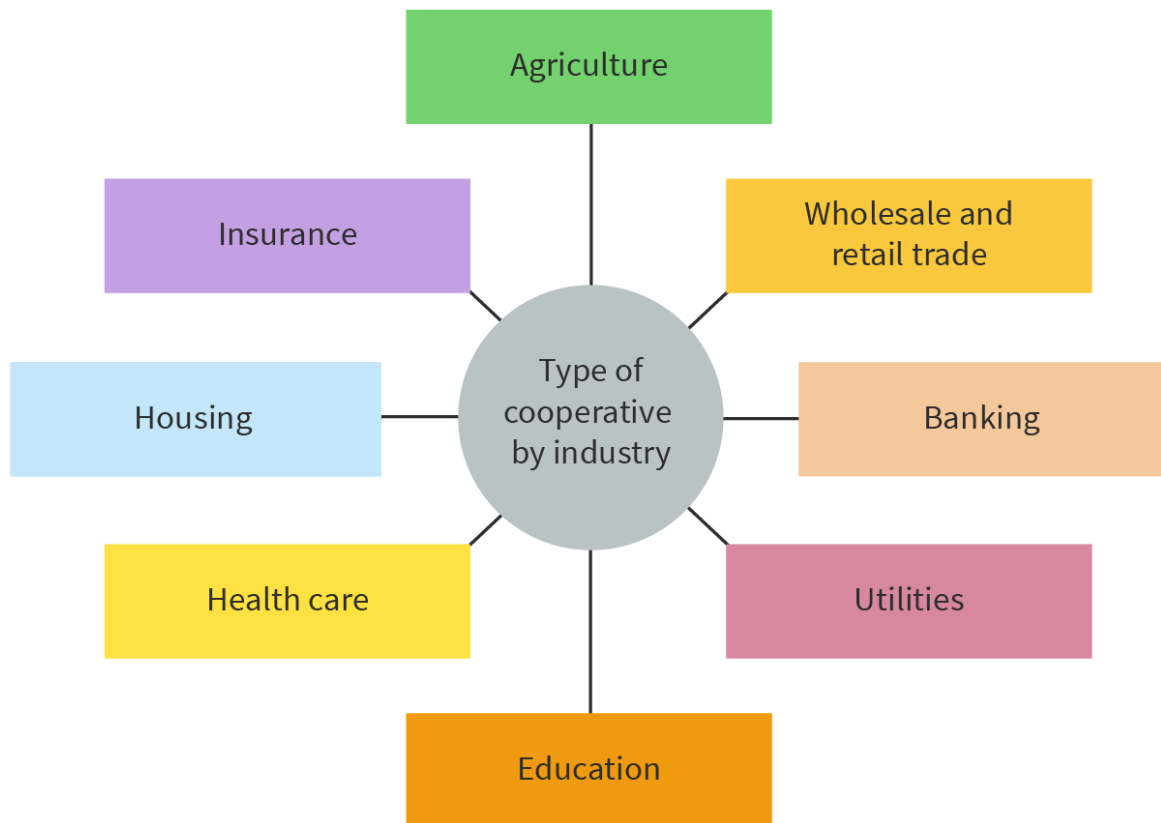
A cooperative is a business that is owned by its members. These members run the organisation in their common interest, using democratic governance. All members participate in decision-making either directly by voting on important decisions or through representation, where members elect representatives to make decisions for them. Cooperatives typically have limited liability. According to the International Cooperative Alliance [🔗](https://www.ica.coop/en/cooperatives/facts-and-figures) (<https://www.ica.coop/en/cooperatives/facts-and-figures>), there are more than three million cooperatives globally and more than 12% of people in the world belong to some type of cooperative. Cooperatives employ about 10% of workers worldwide.

Cooperatives can be classified either by the type of industry or by who owns and runs them. In terms of industries, the 300 largest cooperatives in the world are dominated by insurance, agriculture and wholesale and retail trade. However, cooperatives are also common in other

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industries such as banking, utilities, education, health care, and housing. In terms of ownership, cooperatives may be owned by producers, workers, consumers, residents or multiple stakeholders.



**Figure 3.** Cooperatives by industry.

[More information for figure 3](#)

This diagram shows a central circle labeled "Type of cooperative by industry" with lines connecting it to seven rectangular boxes, each representing a different industry. The industries listed are: Agriculture, Insurance, Wholesale and retail trade, Housing, Banking, Health care, Utilities, and Education. Each box has a distinct background color. The lines are spokes radiating from the central circle, illustrating the various types of industries that cooperatives can belong to.

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You can see the diversity in cooperatives by looking more closely at agricultural cooperatives, which are created for a variety of reasons and can be owned by different stakeholders. Farm owners can form a cooperative to negotiate lower prices on inputs such as fertiliser and seeds by buying in bulk, or by buying expensive equipment together to share. They can also negotiate higher prices for their outputs by working together to equalise power with large grocery retailers. Some may even organise their own credit unions, to offer farmers lower interest rate



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loans when needed. One such credit union, the Credit Agricole in France, is the largest cooperative in the world as of 2021, but has moved far beyond providing banking services to farmers.

Other stakeholders can also own agricultural cooperatives. Workers on an individual farm may form a cooperative to share returns and risk. Agricultural cooperatives can also be owned by a combination of producers and consumers in Community Supported Agriculture (CSA). Through yearly membership/owner fees and monthly payments, consumers can receive a share of the farm's harvest, and they also share the risk. You may even have Community Supported Agriculture in or near where you live.

### Case study

Originating in North Africa, argan trees are now being introduced into other areas that have hot, dry climates. Inside the fruit of the argan tree is a nut containing a kernel (seed), which can be used to produce a rich oil. Argan oil has traditionally been used in medicine, cooking and cosmetics. More recently, argan oil has become a popular export, in demand for use primarily in skincare and haircare products.



**Figure 4.** Argan nuts are used to produce a valuable oil.

Credit: Jeremy Woodhouse, Getty Images

Breaking the argan nuts to reveal the kernels from which oil can be extracted is a difficult process that has not yet been mechanised successfully. So it is done by hand, most often by women. Over the last twenty years or so, cooperatives have been set up to manage the production and sale of argan oil. Women often run these organisations themselves, and may negotiate directly with international buyers of their oil. The cooperatives not only provide employment in rural areas but they also empower women, many of whom are earning incomes for the first time. The development of

  
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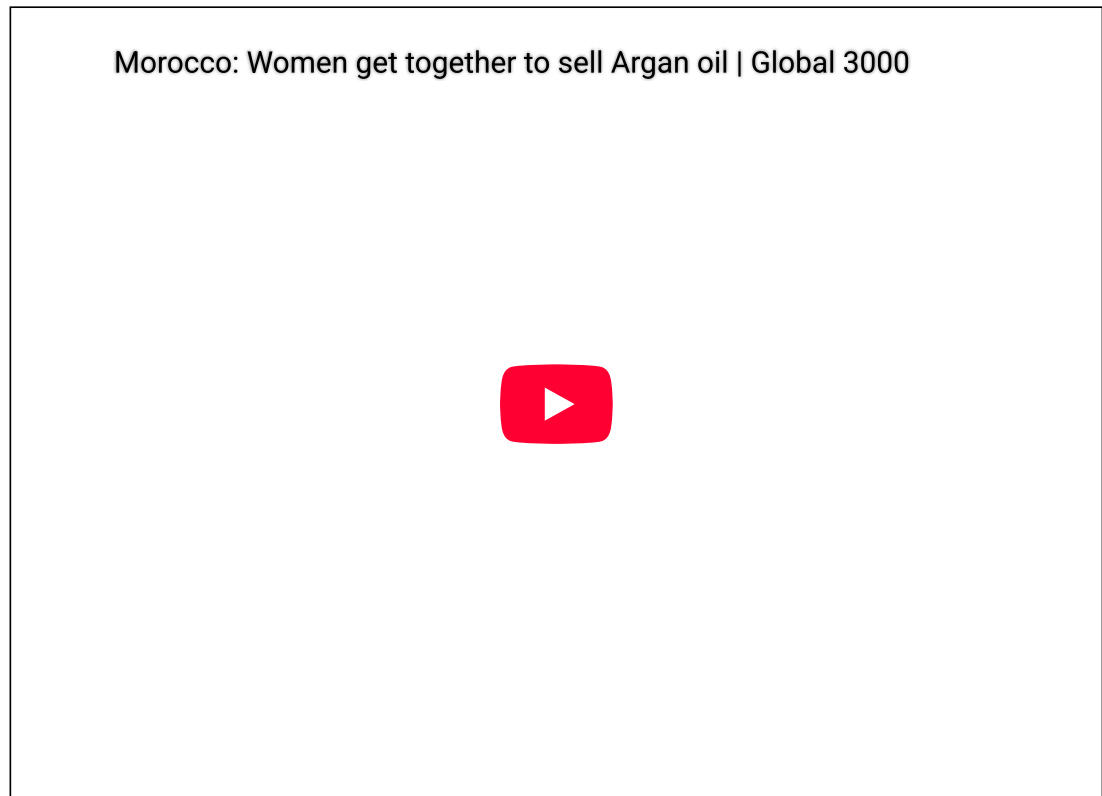


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argan oil also benefits the environment by increasing the value of these trees that protect against desertification and that were previously often cut down for wood. The oil may be priced at the equivalent of 30–50 USD per litre in local areas, but on international markets it can sell for up to 250 USD per litre.

Most argan oil is produced by cooperatives of Berber women near the Moroccan cities of Essaouira, Taroudant and Agadir. The Taitmaitine cooperative near Taroudant employs about 100 women to produce the argan oil. They receive a salary, health insurance, childcare and literacy instruction.

The video below explains how the cooperative started and its operation.



**Video 2.** The Taitmaitine cooperative and how it started.

### Questions

1. Describe the type of cooperative mentioned in the case study. [2 marks]
2. Explain two advantages for the Berber women of this local cooperative. [4 marks]

### Question 1

The type of cooperative mentioned in the case study is an agricultural cooperative. In agricultural cooperatives, farmers pool their financial resources to acquire inputs such as seeds, fertilisers and machinery which can be shared by the members. They can also work together to negotiate lower costs of production for inputs, and to negotiate higher prices for their products. The case study mentions that the Berber women 'negotiate directly with international buyers for their oil'. Because they work together and cut out intermediaries, they are able to retain more income.



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**Describe** is an AO1 level command term requiring a detailed account. Describe *what* something is.

- One mark for correctly identifying the cooperative as an agricultural cooperative and for providing some description.
- One mark for using information from the case study to support the response.
- To achieve full marks, you must always include theory and application to the case study in your responses.

## Question 2

One advantage of agricultural cooperatives is that the members have greater negotiating power with buyers of their products than they would have if working alone. This means that they may be able to sell their products at higher prices and earn more income. The case study mentions that the Berber women 'negotiate directly with international buyers of their oil' and that the oil can fetch up to 250 USD a litre on international markets.

Another advantage of cooperatives generally is that they work for the benefit of their members. This can mean higher incomes and other kinds of benefits needed by the members. The case study mentions that the women in the Taitmaitine cooperative are offered a 'salary, free childcare, health insurance and literacy courses'. The income and benefits are strengthening the social foundation and meeting multiple human needs of the cooperative members.

**Explain** is an AO2 level command term requiring a detailed account including reasons or causes. Explain *why*, explain *how*.

- Only two advantages need to be made.
- Other responses are possible and would be rewarded if appropriate.

To achieve full marks, you must always include theory and application to the case study in your responses.

Section

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Feedback



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## Activity

**Learner profile:** Inquirers

**Approaches to learning:** Research skills (information literacy)

Either individually or in a group, carry out some brief research to find out about other types of cooperatives. Use the table below to record your findings. One example has been provided. Since agricultural cooperatives have been described above, you may want to outline that type of cooperative next in the list before researching the others (insurance, banking, utilities, etc).



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Cooperative industry	Common owners	Common purpose	Examples
Retail	Shopkeepers  Consumers	Negotiate with suppliers, share marketing expenses  Lower prices for members (often consumers work in the business in exchange)	<u>REWE Group</u> ( <a href="https://www.rewe-group.com">https://www.rewe-group.com</a> ) Germany  <u>Coop-Kobe</u> ( <a href="https://www.coop-kobe.net/index.html">https://www.coop-kobe.net/index.html</a> ), Japan  <u>Park Slope Food Coop</u> ( <a href="https://www.foodcoop.com/">https://www.foodcoop.com/</a> ) New York, USA
Agricultural			

## Evaluation of for-profit social enterprises

There are a number of benefits associated with for-profit social enterprises. Firstly, they make a positive impact on the world through their core work, meeting their ethical responsibilities to people and the planet. Secondly, because they generate revenues and profits, for-profit social enterprises are more economically sustainable compared to non-profit social enterprises, which often depend on grants, donations or government financial support that may be unstable. In fact, with for-profit social enterprises, greater positive impact can yield larger profits in a positive feedback loop. And thirdly, for-profit social enterprises attract an increasing number of customers, investors and talented employees who value sustainable and responsible businesses. According to the Economist Intelligence Unit, consumer internet searches for sustainable goods increased globally by 71% from 2016 to 2020, and other studies (<https://www.businesswire.com/news/home/20211014005090/en/Recent-Study-Reveals-More->



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Than-a-Third-of-Global-Consumers-Are-Willing-to-Pay-More-for-Sustainability-as-Demand-Grows-for-Environmentally-Friendly-Alternatives) show that very large majorities of people are shifting their consumption. Thus, there is both a solid ethics and business case for the for-profit social enterprise model.

There are a number of important challenges facing for-profit social enterprises.

## Funding

Like in any business, social entrepreneurs need to find funds to start their work. You will learn more about sources of financing in **Subtopic 3.2**. With social enterprises, investors may need to wait longer to see returns on their investment. Social enterprises often require patient capital, where those providing funding are willing to think more long-term. They may also need to be willing to accept lower returns than might have been typical for a commercial enterprise, as more of the value of the business is distributed to all stakeholders. It is very important that a social enterprise chooses its sources of finance very carefully to ensure that they reflect the purpose and values of the business.



**Figure 5.** For-profit social enterprises need investors willing to take the long view.


Credit: Rich Vintage, Getty Images

## Credibility

Because for-profit social enterprises do not easily fit into traditional models, there may be distrust of the business from a wide range of people. Those connected to the business who are not used to an enterprise making social or environmental purpose part of core operations may



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wonder why the business is not more focused on profit-making. While those who understand and expect the positive purpose may be suspicious of profit-making, wondering whether the enterprise is engaging in **social washing** or **greenwashing** (marketing social or green credentials but not backed up by actions). In any case, it is important that the for-profit social enterprise is transparent, shows full commitment to its cause and embeds ethical practices into all areas of the business. Adopting legal structures or third-party certifications specific to for-profit social enterprises, as mentioned in the [Section 1.2.2 \(/study/app/business-hl/sid-351-cid-762729/book/forprofit-commercial-enterprises-id-36509/\)](#) can help with credibility.

## Measuring impact

Unlike revenue or profits, which can be quantified easily, measuring social or environmental impact is more difficult and may involve qualitative data that is harder to interpret. But gathering data on impact is extremely important for for-profit social enterprises in order to maintain credibility and support from investors and consumers.

## Managing complex supply chains

For businesses that manufacture a physical product, it is important to ensure that all areas of the supply chain are operating in line with the values of the business. As with commercial businesses, for-profit social enterprises may need to [outsource](#) or [offshore](#) part of their production processes. If a supplier exploits labour resources or damages the environment, this can damage the mission and reputation of the business.

## Remaining true to purpose

If a for-profit social enterprise grows its impact, it may be difficult to maintain focus on its purpose. The business may become increasingly complex, with a wider range of stakeholders, including investors, who may have conflicting interests. Changes in external STEEPLE factors ([Section 1.1.6 \(/study/app/business-hl/sid-351-cid-762729/book/tool-swotsteeple-analysis-id-36504/\)](#)) may also require the social enterprise to be flexible and open to change. As it responds to those changes, the business must keep its eye on its purpose.

### Exam tip

Make sure that you are well aware of the challenges facing social enterprises. Especially for HL students, Paper 3 is focused on social enterprise. It is likely that you will be asked to identify and discuss challenges faced by these organisations, and to provide some recommendations about how to overcome them.

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## Activity

**Learner profile:** Thinkers

**Approaches to learning:** Thinking skills (critical thinking)

From the activity and case study presented earlier in this section, select either:

- N'Go
- the Taitmaitine cooperative

Explain some challenges that might be faced by the business you selected, by applying the list of challenges for for-profit social enterprises above in that context.

## 3 section questions ^

### Question 1

Which of the following is **not** a feature of a for-profit social enterprise?

- 1 The business aims to maximise profits for shareholders. ✓
- 2 The business is transparent and accountable to its stakeholders (consumers, investors, government agencies, employees).
- 3 The business's mission is focused on social or environmental objectives.
- 4 The business is generally judged on its impact rather than profits.

### Explanation

For-profit social enterprises do not aim to maximise profits for shareholders. Instead, they aim for an impact on a wide range of stakeholders, which may entail lower profits. Additionally, for-profit social enterprises typically reinvest significant amounts of profit in the business to increase impact, rather than passing all profits to shareholders.

### Question 2

Which of the following **cannot** be a type of for-profit social enterprise?

- 1 Non-governmental organisation (NGO) ✓



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- 2 Sole trader
- 3 Partnership
- 4 Privately held or publicly held companies

### Explanation

For-profit social enterprises can take many forms of legal structure. They can be sole traders, partnerships, or privately or publicly held companies. However, non-governmental organisations are non-profit social enterprises, not for-profit social enterprises.

### Question 3

Which organisations are owned and run democratically by their members?

 Cooperatives



### Accepted answers

Cooperatives , Co-ops, cooperatives, cooperative, co-operatives, co-operative, co-op

### Also accepted

Cooperativas, cooperativa, cooperativas, Cooperatives, corporatives, cooperative, Cooperative industry, cooperatives, coopérative, co-op organisations, Co/ops, coopératives, Coopératives

### Explanation

Cooperatives are organisations that are owned by their members. These members have come together to create and run the organisation in their common interest. An important element of the cooperative form of organisation is their democratic governance.

1. Introduction to business management / 1.2 Types of business entities

# Non-profit social enterprises

Non-profit social enterprise Non-profit social enterprise

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## Main features of non-profit social enterprises

As with a for-profit social enterprise, a non-profit social enterprise works to improve social or environmental outcomes. To qualify for non-profit status, organisations typically need to prove their social or environmental purpose to the government. They may receive all funding through



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grants and donations, or they may be involved in additional revenue-generating activities such as selling goods or services. Any surplus generated is required by law to be reinvested into the business to increase its impact. Most non-profits are run by a board of directors. The board is responsible for hiring senior staff to carry out the organisation's mission. The board is also accountable to third parties, such as the community in which the enterprise operates.

Non-profits are generally classified according to their primary purpose. In addition to universities, many private schools, hospitals and cultural institutions are organised as non-profits, as are religious organisations, political parties, labour unions, professional organisations and some interest groups. Many non-profits exist to help those in need, who may be underserved by government social safety nets or who are marginalised in society.



**Figure 1.** Organisations helping the homeless would be organised as non-profit social enterprises.

Credit: Ariel Skelley, Getty Images

## Evaluation of non-profit social enterprises

In addition to the general benefits and challenges of social enterprises discussed in [Section 1.2.3 \(/study/app/business-hl/sid-351-cid-762729/book/forprofit-commercial-enterprises-id-36509/\)](#), there are a number of benefits specific to the legal structure of non-profit status. Firstly, like corporations, non-profit social enterprises typically have limited liability. This means that the business is a separate legal entity. Secondly, non-profit status requires that all surpluses are reinvested in the enterprise, as opposed to for-profit social enterprises where some of the profits can be paid to owners or shareholders. Because non-profits have to reinvest all surplus, they pay no tax on them. Thirdly, non-profits may be able to rely on volunteers to

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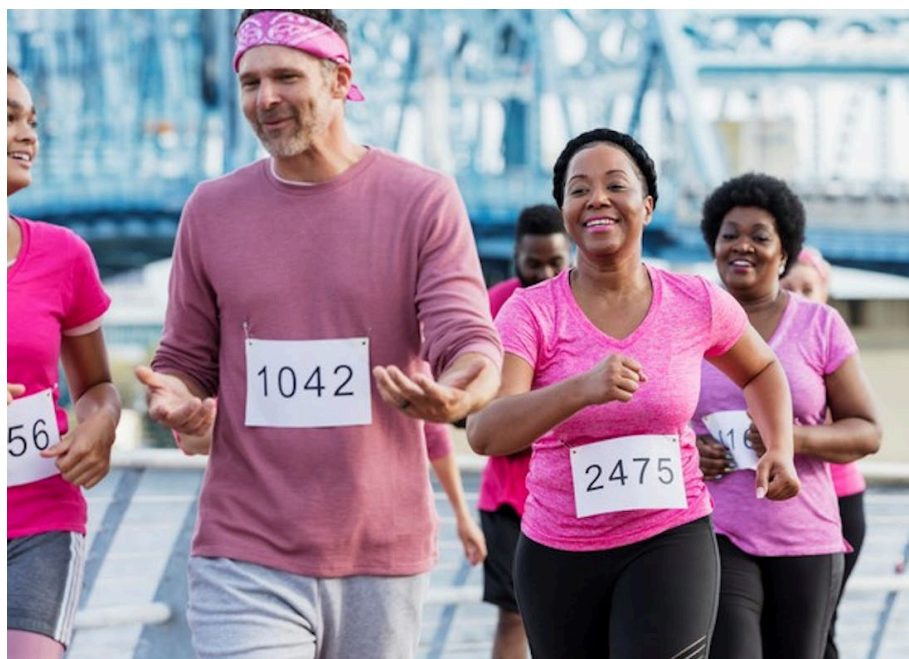


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help with the cause. This can help keep costs low. And finally, non-profits may receive grants and donations, which may not be available to for-profit social enterprises. This increases the range of funding available to non-profit organisations.

Think back to the university example in [Section 1.2.0 \(/study/app/business-hl/sid-351-cid-762729/book/the-big-picture-id-36507/\)](#). You might remember that some universities are organised as non-profit organisations. They can charge tuition fees, accept research grants, and receive donations. All these funds are used to run the institution and invest for the future. Any surplus left after paying expenses is reinvested in the institution. In the case of universities, the accumulated surplus is known as an endowment. Large endowments can earn huge sums in interest every year, contributing to the running of the institution.

However, there are some challenges associated with non-profit status. As with for-profit social enterprises, non-profits can face funding difficulties. And because the non-profit is less likely to be involved in market-based activities, its funding problems may persist over time. Many non-profits have to spend time and energy raising funds from donors or applying for grants; this is time and energy that could be spent on their core purpose. Competition for grants and donations is intense, and these forms of income may be under continuous threat. Because of these persistent funding issues, employee salaries may also be limited, making it difficult to recruit and retain talent. Despite the low pay, however, it is often the case that the motivation and commitment of employees in non-profits is high. Finally, there can be significant paperwork involved in setting up a non-profit organisation. Exemption from tax means that governments need to be very careful about which organisations they grant non-profit status to, and those organisations need to prove that they are meeting social and/or environmental objectives and the legal requirements for reinvesting surpluses.



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## Figure 2. Non-profits may have to spend a lot of time and energy to fundraise.

Credit: kali9, Getty Images

### Theory of Knowledge

Many wealthy individuals have set up non-profit foundations to use their financial assets to improve social and environmental outcomes. This is called philanthropy. A few large or well-known foundations include:

- The Bill and Melinda Gates Foundation (<https://www.gatesfoundation.org/>), from income connected to Microsoft
- The Azim Premji Foundation (<https://azimpremjifoundation.org/>), from income generated from Wipro
- The Chan Zuckerberg Initiative (<https://chanzuckerberg.com/>), from income connected to Facebook
- The Bezos Family Foundation (<https://www.bezosfamilyfoundation.org/>), from income connected to Amazon
- The Li Ka Shing Foundation (<https://lksf.org/>), from income connected to CK Hutchison Holdings

There is no doubt that these foundations have done enormous good in the world. However, there are critics who claim that these well-funded institutions can undermine society and political institutions, creating ethical issues that need to be addressed.

Read this interview (<https://news.stanford.edu/2018/12/03/the-problems-with-philanthropy/>) with Stanford University scholar Rob Reich, who has written extensively about this topic.

- Which ethical issues associated with philanthropy does Reich highlight?
- How might those ethical issues be amplified if the money used to fund the foundation is earned through a business that has used aggressive tax avoidance measures in the countries where it operates?

## Non-governmental organisations (NGOs)

Non-governmental organisations (NGOs) are a sub-category of non-profit social enterprises that have a purpose or mission to benefit society or the environment. As the name implies, NGOs are not controlled by governments however they can receive government funding. Although the term NGO is used loosely around the world, it often refers to groups whose work has a broad



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scale, usually national or international, and where the work may overlap with activities in which governments engage. That is why there is a need to distinguish them from government activities, through the label 'NGO'.

NGOs are involved in a wide range of activities, as shown in **Table 1**.

**Table 1.** Examples of non-governmental organisations and their area of focus.

Organisation	Area of focus	Global / National
<u>Amnesty International</u> ( <a href="https://www.amnesty.org/en/">https://www.amnesty.org/en/</a> )	Human rights	Global
<u>Wikimedia Foundation</u> ( <a href="https://wikimediafoundation.org/">https://wikimediafoundation.org/</a> )	Open information	Global
<u>Médecins Sans Frontières</u> ( <a href="https://www.msf.org/">https://www.msf.org/</a> )	Medical care in conflict zones and low-income countries	Global
<u>Acumen Fund</u> ( <a href="https://acumen.org/">https://acumen.org/</a> )	Impact investments	Global
<u>Goonj</u> ( <a href="https://goonj.org/">https://goonj.org/</a> )	Disaster relief, humanitarian aid, community development	National (India)
<u>Rioterra</u> ( <a href="http://rioterra.org.br/pt/">http://rioterra.org.br/pt/</a> )	Amazon reforestation	National (Brazil)
<u>ANTaR</u> ( <a href="https://antar.org.au/">https://antar.org.au/</a> )	Justice, rights and respect for Australia's First Peoples	National (Australia)



## Activity

**Learner profile:** Thinkers

**Approaches to learning:** Thinking skills (critical thinking, transfer)

The Bill and Melinda Gates Foundation was set up in 1997 to fight poverty, disease and inequality. The foundation was set up by Microsoft founder Bill Gates. Warren Buffet, another of the most wealthy people in the world, is also a major contributor to the foundation, which had an endowment of about 50 billion USD in 2021.

Watch the video below to learn more about the foundation and its activities.



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## What does the Bill and Melinda Gates Foundation do?



**Video 1.** How the Bill and Melinda Gates Foundation started and the work that it has done.

Consider the benefits and challenges of social enterprises generally, discussed in [Section 1.2.3 \(/study/app/business-hl/sid-351-cid-762729/book/forprofit-social-enterprises-id-36510/\)](/study/app/business-hl/sid-351-cid-762729/book/forprofit-social-enterprises-id-36510/), and specifically of non-profit social enterprises in this section.

To what extent do those benefits and challenges apply to the Bill and Melinda Gates Foundation, a very large, very well-endowed non-profit social enterprise?

## 3 section questions ▾

1. Introduction to business management / 1.2 Types of business entities

# Terminology exercise

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**Check that you understand the terminology used in this subtopic by dragging the correct word into each space.**

Businesses in the \_\_\_\_\_ are owned and controlled by private individuals; the government might have little involvement in their decision-making. Businesses in the \_\_\_\_\_ are owned and run by the government; their role is to provide essential services for the people, such as free or subsidised healthcare and education. The \_\_\_\_\_ sector provides for human needs, usually by providing wide access to services.

\_\_\_\_\_ are individuals who own and run their businesses alone; there is little legal distinction between the individual and their business. They also have \_\_\_\_\_, which means they are personally responsible for any business debts and may have to sell their personal assets to pay back any debt. A \_\_\_\_\_ refers to a business alliance between two or more individuals who are jointly responsible for the business.

\_\_\_\_\_ are generally large organisations owned by many individuals and groups of individuals, known as \_\_\_\_\_. A \_\_\_\_\_ company has greater finance available because there are many people who can invest in the business. Shares are sold for the first time at the initial \_\_\_\_\_, where the business sells all or part of the business to external shareholders. As owners of the business, the shareholders usually receive a portion of the profits in the form of \_\_\_\_\_.

shareholders   public   dividends   public sector   private sector   Sole traders  
unlimited liability   Companies   partnership   publicly held   public offering

✓ Check



Question: 1 of 2 questions

## Interactive 1. Understanding Business Sectors and Ownership Structures.

1. Introduction to business management / 1.2 Types of business entities

# Checklist



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## What you should know

By the end of this subtopic, you should be able to:

- define the following terms: (AO1)
  - private sector
  - public sector
  - sole trader
  - partnership
  - publicly held company
  - privately held company
  - for-profit social enterprise
  - cooperative
  - non-profit social enterprise
  - non-governmental organisation (NGO)
- distinguish between the private and public sectors (AO2)
- compare and contrast the sole trader, partnership and corporation forms of ownership (AO3)
- examine different forms of for-profit and non-profit social enterprises (AO3)
- recommend an appropriate type of legal structure for a business (AO3)

1. Introduction to business management / 1.2 Types of business entities

# Reflection

Section

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## Teacher instructions

The goal of this section is to encourage students to pause at the end of the subtopic and to reflect on their learning. Students can use the questions provided below to guide their reflection. The questions encourage students to look at the bigger picture and to consider how the subtopic's contents might have impacted the way they view the subject.



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The following table shows you how each prompt aligns to the DP *Business management* guide:

Prompt #	Syllabus alignment
1	<b>Concept:</b> Ethics
2	<b>Learner profile:</b> Balanced
3	<b>Concept:</b> Sustainability

Students can submit their reflections to you by clicking on 'Submit'. You will then see their answers in the 'Insights' part of the Kognity platform.



## Reflection

In this subtopic you looked at different types of businesses and their characteristics.

Take a moment to reflect on your learning so far. You can use the following questions to guide your reflection. If you click 'Submit', your answers will be shared with your teacher.


1. Does a publicly held company have different ethical obligations to a privately held company?
2. In your opinion, should some businesses be controlled by the government while others are controlled privately? To what extent are your opinions shaped by your lived experiences?
3. When examining social enterprises, social or environmental impacts, such as sustainable outcomes, may be more difficult to measure accurately. Does this mean they are worthless?

⚠ Once you submit your response, you won't be able to edit it.



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### Rate subtopic 1.2 Types of business entities

Help us improve the content and user experience.



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