Lecture 3

BUSINESS ORGANIZATION & SOLE PROPRIETORSHIP

Business organization is an act of grouping activities into effective cooperation to obtain the objective of the business.

In the words of L. H. Haney

“It is more or less independent complex of land, labour and capital, organized and directed for productive purposes but entrepreneurial ability.”

SCOPE OF BUSINESS ORGANIZATION

The scope of business organization can be defined as under:

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1. SOLE PROPRIETORSHIP

According to D.W.T. Stafford

“It is the simplest form of business organization, which is owned and controlled by one man”

Sole proprietorship is the oldest form of business organization which is owned and controlled by one person. In this business, one man invests his capital himself. He is all in all in doing his business. He enjoys the whole of the profit. The features of sole proprietorship are:

- Easy Formation
- Unlimited Liability
- Ownership
- Profit
- Management
- Easy Dissolution
2. PARTNERSHIP

According to Partnership Act, 1932

“Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.”

Partnership means a lawful business owned by two or more persons. The profit of the business shared by the partners in agreed ratio. The liability of each partner is unlimited. Small and medium size business activities are performed under this organization. It has the following features:

- Legal Entity
- Profit and Loss Distribution
- Unlimited Liability
- Transfer of Rights
- Management
- Number of Partners

3. JOINT STOCK COMPANY

According to S. E. Thomas

“A company is an incorporated association of persons formed usually for the pursuit of some commercial purposes”

A joint stock company is a voluntary association of persons created by law. It has a separate legal entity apart from its members. It can sue and be sued in its name. In the joint stock company, the work of organization begins before its incorporation by promoters and it continues after incorporation. The joint stock company has the following feature:

- Creation of Law
- Separate Legal Entity
- Limited Liability
- Transferability of shares
- Number of Members
- Common Seal

4. COOPERATIVE SOCIETIES

According to Herrick

“Cooperation is an action of persons voluntarily united for utilizing reciprocally their own forces, resources or both under mutual management for their common profit or loss.”
Cooperative Societies are formed for the help of poor people. It is formed by economically weak persons of the society. In this form of organization, all members enjoy equal rights of ownership. The features of cooperative society are as under:-

- Easy Formation
- Protection of Mutual Interest
- Limited Liability
- Equal Distribution of Wealth
- Equal Rights

5. COMBINATION

According to J. L. Hanson

“Combination is the association, temporary or permanent, of two or more firms.”

Business combinations are formed when several business concern undertaking units are combined to carry on business together for achieving the economic benefits. The combination among the firms may be temporary or permanent. The salient features of business combination are:

- Economy in Production
- Effective Management
- Division of Labour
- Destructive Competition

IMPORTANCE OF BUSINESS ORGANIZATION

The following points elaborate the role of business organizations:

1. Distribution

Another benefit of business organization is that it solves the problems of marketing and distribution like buying, selling, transporting, storage and grading, etc.

2. Feedback

An organization makes possible to take decisions about production after getting the feedback from markets.

3. Finance Management

It also guides the businessman that how he should meet his financial needs which is very beneficial for making progress in business.
4. **Fixing of Responsibilities**

It also fixes the responsibilities of each individual. It introduces the scheme of internal check. In this way chances of errors and frauds are reduced.

5. **Minimum Cost**

It helps in attaining the goals and objectives of minimum cost in the business.

6. **Minimum Wastage**

It reduces the wastage of raw material and other expenditures. In this way the rate of profit is increased.

7. **Product Growth**

Business organization is very useful for the product growth. It increases the efficiency of labor.

8. **Quick Decision**

Business organization makes it easy to take quick decisions.

9. **Recognition Problems**

Business organization makes it easy to recognize the problems in business and their solutions.

10. **Reduces the Cost**

Business organization is useful in reducing the cost of production as it helps in the efficient use of factors of production.

11. **Secretariat Functions**

It also guides the businessman about the best way of performing the secretarial functions.

12. **Skilled Salesmen**

It is also a benefit of the business organization that it provides the skilled salesmen for satisfying various needs of the customers.
13. Transportation

It is another benefit is that it guides the businessman that what type of transport he should utilize to increase the sales volume of the product.

PRE-REQUISITES OF BUSINESS

Following are the main pre-requisites of a successful business:

1. Selection

The first and most important decision before starting a new business is its selection. If once a business is established, it becomes difficult to change it. One should make a detailed investigation in the selection of business.

2. Feasibility Report

A person should prepare the feasibility report about the business to be started. This report will provide the facts and figures whether business is profitable or not.

3. Nature of Business

There are various types of business like manufacturing, trading and services. The businessman should decide that what type of business he would like to start.

4. Demand of Product

The businessman also keeps in view the demand of the product which he wants to sell. If the demand is inelastic, the chances of success are bright. If the demand of a product is irregular, seasonal and uncertain, such business should not be started.

5. Size of Business

The Size of business means the scale of business. The size of business depends upon the demand of commodity in the market and organizational ability of entrepreneur. The determination of size of business is an important decision of a person.
6. **Availability of Capital**

Availability of capital is an important factor in the business. Capital is required for the purchase of land, machines, wages and raw materials. A businessman must decide that how much capital he can arrange.

7. **Business Location**

A businessman has to select the place where he wants to start his business. He should select that place where raw material, cheap labour and transportation facilities are available. He should also check the location of business competitors.

8. **Government Policy**

The businessman should also carefully consider the policies of government before starting a new business. Some areas are declared as ‘tax free zones’ and for some particular businesses the loan is provided without any interest.

9. **Availability of Raw Material**

Availability of Raw material is essential to produce the goods at low cost. Sometimes the raw material is to be imported which may create problem for him. So a businessman must keep this factor in mind.

10. **Availability of Machines**

Availability of new machines is also an important factor for a business. A businessman must see whether these machines are easily available inside the country or not. If these are to be imported then it may create the problems for him.

11. **Availability of Labor**

Skilled and efficient labor is essential to run the business in profit. But if efficient and skilled labor is not available where business is going to be started then it will not be profitable.

12. **Means of Transportation**

Quick and cheap means of transportation are essential for low cost of production and high profit rate. A businessman must keep in view this factor.

13. **Power Resources**

There must be availability of power resources like water, oil, coal and electricity. So businessman must keep in view this factor.
14. Hiring Employees

A businessman must hire the efficient and competent employees in the business. The proper training must be given to employees.

15. Product Pricing

A businessman must decide the price of his product. In the beginning the price must be low. He must keep in view that whether he will cover cost of his product and other expenses with such price.

FUNCTIONS OF BUSINESS

Following are the main functions of a business:

1. Production

Production of goods and services is the first main function of the business. The production must be regular. The goods and services must be produced in such a way which can satisfy human needs.

2. Sales

The sale is another important function of the business. Sales are of two types:

- Cash sales
- Credit sales

The sale must be regular and at reasonable price. It is very difficult job because there is hard competition in each market.

3. Finance

It is also an important function of the business to secure finance. Finance is required for establishment and expansion of business. There are two sources of raising funds:

(a) Owner’s Capital
(b) Borrowed Funds
4. Management Function

“To do things efficiently and effectively” is known as management. The functions of management are:

- Planning
- Organizing
- Leading
- Controlling
- Staffing

The management also provides direction for all subordinates.

5. Innovation

In this era of competition, for the survival of business, innovation is essential. The businessman must try to find new techniques of production because the business may not sell present output in future.

6. Accounting

Another function of the business is to maintain its records properly. To record the business activities is called accounting. With proper accounts, the owner can know the actual performance of business and chances of fraud are reduced.

7. Marketing

According to Harry Henser

“Marketing involves the design of the products acceptable by the consumers and the conduct of those activities which facilitate the transfer of ownership between seller and buyer.”

Through marketing, goods are moved from producers to consumers. It is an important function of the business. This function includes buying, selling, transportation, product designing and storage, etc. The concept of marketing mix is very important in marketing. It includes four Ps:

- Product
- Price
- Place
- Promotion
8. Quality Improvement

Quality of product must be improved to increase the sale. If quality of product is poor then business may suffer a loss.

9. Motivation

Motivation is very essential for increasing the efficiency of employees. Motivation encourages the employees to give their best performance.

10. Research

Research is also an important function of any business. Research is a search for new knowledge. By research, business becomes able to produce improved and new goods. The research is of two types:

- Basic Research
- Applied Research

11. Public Relation

It is very important function to make friendly relations with public, in this way sales volume is increased.

SOLE PROPRIETORSHIP

Sole Proprietorship and its Characteristics

Sole proprietorship is a simple and oldest form of business organization. Its formation does not require any complicated legal provision like registration etc. It is a small-scale work, as it is owned and controlled by one person, and operated for his profit. It is also known as “sole ownership”, “individual partnership” and “single proprietorship”.

DEFINITION

Following are some important definition of sole proprietorship:

1. According to D.W.T. Stafford

   “It is the simplest form of business organization, which is owned and controlled by one man.”
2. According to G. Baker

“Sole proprietorship is a business operated by one person to earn profit.”

CHARACTERISTICS

Following are the main characteristics of sole proprietorship:

1. Capital

In sole proprietorship, the capital is normally provided by the owner himself. However, if additional capital is required, such capital can be increased by borrowing.

2. Easy Dissolution

The sole proprietorship can be easily dissolved, as there are no legal formalities involved in it.

3. Easily Transferable

Such type of business can easily be transferred to another person without any restriction.

4. Freedom of Action

In sole proprietorship, single owner is the sole master of the business; therefore, he has full freedom to take action or decision.

5. Formation

Formation of sole proprietorship business is easy as compared to other business, because it does not require any kind of legal formality like registration etc.

6. Legal Entity

In sole proprietorship, the business has no separate legal entity apart from the sole traders.

7. Legal Restriction

There are no legal restrictions for sole traders to set up the business. But there may be legal restrictions for setting up a particular type of business.

8. Limited Life

The continuity of sole proprietorship is based on good health, or life or death of the sole owner.
9. **Management**

In sole proprietorship, the control of management of the business lies with the sole owner.

10. **Ownership**

The ownership of business in sole proprietorship is owned by one person.

11. **Profit**

The single owner bears full risk of business, therefore, he gets total benefit of the business as well as total loss.

12. **Size**

The size of business is usually small. The limited ability and capital do not allow the expansion of business.

13. **Success of Business**

The success and goodwill of the sole proprietorship is totally dependent upon the ability of the sole owner.

14. **Secrecy**

A sole proprietorship can easily maintain the secrecy of his business.

15. **Unlimited Liability**

A sole proprietor has unlimited liability. In case of insolvency of business, even the personal assets are used by the owner to pay off the debts and other liabilities.

**ADVANTAGES OF SOLE PROPRIETORSHIP**

Following are the advantages of sole proprietorship:

1. **Contacted with the Customers**

In sole proprietorship a businessman has direct contact with the customer and keeps in mind the like and dislikes of the public while producing his products.

2. **Direct Relationship with Workers**

In sole proprietorship a businessman has direct relationship with workers. He can better understand their problems and then tries to solve them.
3. **Easy Formation**

Its formation is very easy because there are not legal restrictions required like registration etc.

4. **Easy Dissolution**

Its dissolution is very simple because there are no legal restrictions required for its dissolution and it can be dissolved at any time.

5. **Easy Transfer of Ownership**

A sole proprietorship can easily be transferred to other persons because of no legal restriction involved.

6. **Entire Profit**

Sole proprietorship is the only form of business organization where the owner enjoys 100% profit.

7. **Entire Control**

In sole proprietorship the entire control of the business is in the hands of one person. He can do whatever he likes.

8. **Flexibility**

There is great flexibility in sole proprietorship. Business policies can easily be changed according to the market conditions and demand of people.

9. **Honesty**

The sole master of the business performs his functions honesty and efficiently to make the business successful.

10. **Independence**

It is an independent form of business organization and there is no interference of any other person.

11. **Personal Satisfaction**

As all the Business activities are accomplished under the supervision of sole owner, so he feels personal satisfaction that the business is running smoothly.
12. **Prime Credit Standing**

A sole proprietor can borrow money more easily because of unlimited liability.

13. **Quick Decisions**

Sole proprietor can make quick decisions for the development and welfare of his business and in this way can save his time.

14. **Personal Interest**

A sole proprietor takes keen interest in the affairs of business because he alone is responsible for profit and loss.

15. **Saving in Interest on Borrowed Capital**

Sometimes, a sole proprietor borrows money to increase his capital, from his relatives, without interest.

16. **Saving in Legal Expenses**

As there are no legal restrictions for the formation of sole proprietorship so it helps in increasing savings as legal expenses are reduced.

17. **Saving in Management Expenses**

The owner of the business himself performs most of the functions so it reduces the management expenses.

18. **Saving in Taxes**

The tax rates are very low on sole proprietorship because it is imposed on the income of single person.

19. **Secrecy**

It is an important factor for the development of business. A sole trader can easily maintain the secrecy about the techniques of production and profit.

20. **Social Benefits**

It is helpful in solving many social problems like unemployment etc.
DISADVANTAGES OF SOLE PROPRIETORSHIP

The disadvantages of sole proprietorship can be narrated as under:

1. **Continuity**

   The continuity of sole proprietorship depends upon the health and life of the owner. In case of death of the owner the business no longer continues.

2. **Chances of Fraud**

   In sole proprietorship, proper records are not maintained. This increases the chances of errors and frauds for dishonest workers.

3. **Expansion Difficulty**

   In sole proprietorship, it is very difficult to expand the business because of the limited life of proprietor and limited capital.

4. **Lack of Advertisement**

   As the sources of single person are limited so he cannot bear the expense of advertisement, which is also a major disadvantage.

5. **Lack of Capital**

   Generally, one-man resources are limited, so due to financial problems he cannot expand his business.

6. **Lack of Inspection and Audit**

   In sole proprietorship there is lack of inspection and audit, which increases the chances of fraud and illegal operations.

7. **Lack of Innovation**

   Due to fear of suffering from loss, a sole proprietor does not use new methods of production. So, there is no invention or innovation.

8. **Lack of Public Confidence**

   The public shows less confidence in this type of business organization because there is no legal registration to control and wind up the business.
9. Lack of Skilled Persons

One person cannot hire the services of qualified and skilled persons because he has limited resources. It is also a great disadvantage.

10. Management Difficulty

One person cannot perform all types of duties effectively. If he is a good accountant, he may not be a good administrator. Due to this, business suffers a loss.

11. Much Strain on Health

In this type of business organization there is much strain on the health of the businessman because he alone handles all sorts of activities.

12. Not Durable

This type of business organization is not durable because its existence depends upon the life of sole proprietor.

13. Permanent Existence

In this type of business there is a need of permanent existence of a businessman. In case of absence from business for few days may become the cause of loss.

14. Risk of Careless Drawings

In sole proprietorship, owner himself is a boss. There is no question to his decisions or actions. So, there is a risk of careless drawings by him.

15. Risk of Loss

In case of sole proprietorship a single person bears all the losses, whereas in the case of partnership or Joint Stock Company all the partners or members bear the loss.

16. Unlimited Liability

In sole proprietorship there is unlimited liability. It means, in case of loss personal property of the owner can be sold to satisfy the claimants. It is a great disadvantage.
CONCLUSION

From the above-mentioned detail, we come to the point that despite the above disadvantages, sole proprietorship is an important form of business organization. This is due to the fact that its formation is very easy and due to unlimited liability the owner takes great care and interest in the business, because in case of loss, he is personally responsible. As he enjoys entire profit, this factor also encourages him to work with great efficiency which promotes his business.