June 2019

ECO-01 Business Organisation

Note : Attempt any five questions. All questions carry equal marks.

1. Distinguish between the following : (5+5)

(a) Ownership capital and Borrowed capital.

Ans: Ownership capital refers to the capital collected by issuing various types of shares. On the other hand, borrowed capital refers to the capital collected by issuing debentures, bonds, taking loans from banks etc. Ownership capital is a permanent capital, as the company is not under obligation to repay the amount during its lifetime. Whereas, borrowed capital is a temporary capital as it is to be repaid after fixed period. Ownership capital is mentioned in capital clause of memorandum of Association. Contrarily, borrowed capital is not mentioned in memorandum of Association. In the case of ownership capital, return on capital is paid in the form of dividend whereas in borrowed capital, return of capital is paid in the form of interest. Ownership capital is not a liability for a company, whereas borrowed capital is a liability for a company. Ownership capital is used for acquiring fixed assets and borrowed capital is used to acquire current assets.

(b) Business and Commerce

Ans:

Business	Commerce
Business refers to all those activities which are done with the aim of earning profits.	Commerce refers to all activities which facilitates the exchange of goods from producer to end consumer.
Huge amount of capital is needed.	Requires less capital.
It is a connectivity between owner and client.	It is connectivity between producer and consumer.
Business is a wider concept.	It is just a part or a subset of business.
It focuses on planning, advertising, selling, marketing, accounting and supervising manufacturing.	It focuses on buying and selling part of a business

2. Explain the concept of 'Business' and describe the objectives of business. (5+5)

Ans: Business: Business refers to the human activities engaged in production and/or exchange of want satisfying goods and services carried with the intention of earning profits.

Any activity carried primarily with the object of earning profit can be called a business activity. This objective of earning profit is achieved by production and/or exchange of want satisfying goods and services. Therefore, we can define business as "any activity concerned with the production and/or exchange of want satisfying goods and services carried with a view of earning profit". Production of soaps, sale of eggs, production of TV sets, transport, etc., are some examples of business. A person who

is engaged in business is called a businessman or entrepreneur. Similarly, a firm formed for the purpose of carrying a business activity is called a business enterprise or a business firm.

Five broad features of business are:

* Dealings in goods and services: Business deals with goods and services. The goods may be consumer goods such as sweets, bread, cloth, shoes, etc. They may be producer's goods such as machinery, equipment, etc., which are used to produce further goods for consumption. Business also deals with services such as transport, warehousing, banking, insurance, etc., which are intangible and invisible goods.

* Production and/or exchange: An economic activity is called a 'business' only when there is production or transfer or exchange or sale of goods or services for value. If goods are produced for self consumption or presentation as gift, such activities are not to be treated as business. In a business activity, there are two parties i.e., a buyer and a seller. Such activity should concern with the transfer of goods or exchange of goods between a buyer and a seller. The goods may be bartered or exchanged for money.

* Continuity and regularity in dealings: A single transaction is not treated as business. An activity is treated as business only when it is undertaken continually or at least recurrently. For example, if a person sells his residential house, it is not considered as business. If he repeatedly buys houses and sells to others, such activity comes under business. But how frequently the transaction should occur depends on the nature of the activity.

* Profit motive: Earning profit is the primary motive of business. A business will flourish only when it is able to serve its customers to their satisfaction. Profits are essential to enable the business to survive, to grow, expand, and to get recognition.

* Element of Risk: In every business, there is a possibility of incurring loss. This possibility of incurring loss is termed as risk. The element of risk exists due to a variety of factors which are outside the control of the business enterprise. There are two kinds of risks. (I) Risks whose probability can be calculated and can be insured. Losses due to fire, floods, theft, etc., are some examples. (2) Risks whose probability cannot be calculated and which cannot be insured against, e.g., changing technology, fall in demand, changing fashions, short supply of raw materials, etc. These risks are to be completely born by the enterprise.

Objectives of business:

The primary objective of business is to earn profit. Although profit plays an important role as a criterion of success, business may not exist for long with the sole objective of earning profit. Thus, serving the community is regarded as another important objective of business.

The objectives of business could be listed under three broad headings: (1) economic objectives, (2) social objectives, and (3) human objectives.

Economic Objectives: Basically, being an economic activity, primary objectives of business are economic. Some of the main economic objectives are:

i) Earning of satisfactory profits.

ii) Exploring new markets and creation of more customers.

iii)Growth and expansion of business operations of the firm.

iv)Making innovations and improvements in goods and services so that customers get improved and more economic goods and services.

Social Objectives: Business, being a part of the society, has obligations towards the society also. Some major social objectives are:

i)Providing more and more employment opportunities to the people in the country.

ii) Supply of quality goods to the community.

iii) Providing goods at reasonable prices.

iv) Ensure fair returns to investors.

v) Avoidance of profiteering and unfair practices.

vi) Production of goods in accordance with national interests and priorities.

Human Objectives: Business activity is, generally, carried out through employees who are human beings. In fact, the efficiency and the success of the business enterprise depends on the motivation and ability of its employees. Therefore, business must also have some human objectives to safeguard the interests of its employees. Some of the major human objectives are:

i)Fair deal to employees in terms of wages and incentives.

ii)Providing better working conditions and environment to the employees.

iii)Provide job satisfaction.

iv) Provide the employees more and more' promotional/growth opportunities.

3. What is cooperative form of business organisation ? Explain the features of a cooperative form of organisation.(5+5)

Ans: Cooperative organisations are generally started by the poor and the economically weak sections to promote their common economic interests through business propositions. The primary objective of any cooperative organization is to render service to its members. The important features of the cooperative organization are service in place of profit, mutual help in place of competition, self-help in place of dependence and moral solidarity in place of unethical business practices.

A cooperative society is a voluntary association of persons and not of capital. Any person can join a cooperative society of his free will and can leave it at any time. This has two important connotations:
i)Any person can become a member irrespective of his caste, creed, religion, colour ,sex etc.

ii)The members come together to form themselves into an association without any coercion or intimidation.

A cooperative society is a self-governing organisation. It is self-sufficient, self renewing, and self controlling within its jurisdiction. A cooperative organisation also enjoys a separate and independent entity distinct from that of its members. It has a perpetual life and is not affected by the entry and exit

of members. In cooperative system, profits are distributed among the shareholders for the capital they have contributed. But the rate of dividend paid to the shareholders is limited to 9% as per the Cooperative Societies Act.

Features of Cooperative form of organisation:

1. Voluntary Association: A cooperative so-ciety is a voluntary association of persons and not of capital. Any person can join a cooperative society of his free will and can leave it at any time. This has two important connotations:

i)Any person can become a member irrespective of his caste,creed,religion,colour,sex etc.

ii)The members come together to form themselves into an association without any coercion or intimidation.

2. Democratic Management: An individual member is considered not as a capitalist but as a human being and under cooperation, economic equality is fully ensured by a general rule—one man one vote. Irrespective of the number of shares held by any member, all enjoy equal rights and equal duties.

3. Capital: Capital of a cooperative society is raised from members through share capital. Cooperatives are formed by relatively poorer sections of society; share capital is usually very limited. The major part is raised either by way of loan from the government and the central cooperative banks.

4. Autonomy and stability: A cooperative society is a self-governing organisation. It is self-sufficient, self renewing, and self-controlling within its jurisdiction. A cooperative organisation also enjoys a separate and independent entity distinct from that of its members. It has a perpetual life and is not affected by the entry and exit of members.

5. Service motive: The primary objective of any cooperative society is to provide service to its members.

6. Limited return on capital: In cooperative system, profits are distributed among the shareholders for the capital they have contributed. But the rate of dividend paid to the shareholders is limited to 9% as per the Cooperative Societies Act.

7. Distribution of surplus: In case of cooperative societies, after giving a limited dividend to shareholders, the surplus profits are distributed in the form of bonus.

4. What are the various types of business risks ? Discuss the various steps involved in risk management. (4+6)

Ans: Pure and Speculative risks

The occurance of perils like fuel windstorm, explosion, flood, earthquake, riot, etc., generally cause losses only. Their occurance never result into gains. The uncertainty concerning their occurance may be termed as pure risks. Thus, Pure risks are those risks in which tlie occurance of events causes losses only. For instance, car drivers always face the risk of accidents. If an accidence occurs, the driver may suffer physical and financial losses. If the accident did not occur, there would not be any gain. Thus, in the case of a pure risk, there is loss when it occurs, otherwise , there is no loss or gain. On the other hand speculative risks involve events which may produce either gains or losses. For instance, expansion of operations in a new market (area] may lead to higher profits or loss of invested funds. Most business

decisions relating marketing, production, finance, etc., are taken with the idea of making gains, but there are possibilities of incurring losses also. Thus, all business enterprises face both pure risks as well as speculative risks. Many pure risks can be handled through insurance, while most of the speculative risks are not generally handled through insurance. So business enterprises must find their own ways of handling specualtive risks.

Static and Dynamic Risks

Risks can also be classified as dynamic risks and static risks. Dynamic risks are related to uncertainties caused by an ever-changing business environmental factors such as consumer wants, technology, competition, governmental policies, firms internal organisation, etc. On the other hand static risks are those which occur even if there are no changes in the business environment. Normally static risks are closely related to pure risks such as fire, flood, windstorm, etc., whereas dynamic risks are more closely associated with speculative risks. Most of the static risks can be handled through insurance while most of the dynamic risks may not be handled by insurance.

Risk Classified by Loss Severity

Risks may also be classified as follows into three groups on the basis of the extent of loss and its importance on the financial position of the business firm:

Class 1: Those losses which do not disturb a firms basic finances.

Class 2: Those losses which would require borrowing or selling firms property.

Class 3: Those losses which might bankrupt the firm.

Class 1 risks cause small losses, Class 2 risks cause much bigger losses, and the firm may not survive with the occurrence of Class 3 risks. Therefore, Class 1 and 2 risks can be handled by various internal methods but Class 3 risks are beyond internal capabilities of the business firms.

Objective and Subjective Risks

Objective risk is the measure of the degree of variation in the proportion of actual from the expected events. This proportion declines at the number of observed events increase. Hence, the objective risk as a proportion declines when larger and larger number of events are involved. Subjective risk may be defined as the uncertainty of an event as seen or perceived by an individual. This perception depends on the attitudes of the concern individuals towards risk. Among people, there are 'risk lovers' who prefer a situation with a great deal of uncertainty, and also 'risk haters' or 'risk averters' who do not like to face risks.

Risk management involves five basic steps:

i) Risk identification is the first step and also the most difficult function. Failure to identify all the loss exposers of the firm means you will not be in a position to deal with those risks.

ii) After identifying the risks, next step is to assess the intensity of financial loss associated with each of those risks. We have to determine two aspects: I) probability of the occurrence of each of the perils or risk identified in the first stage, and II) extent of financial loss to the firm, if that peril occur. With this assessment, we can identify the relatively more serious risks and pay more attention to them.

iii) Third step is to decide on various tools of risk management and decide upon the best combination of the tools to be used. There are six tools for risk management :

I)assumption(or retension)

II) loss prevention

III)avoidance

IV)transfer(insurance)

V)separation

VI)combination

I) Risk assumption or retention: This is a common way of handling risks. Business enterprises assume or retain risks consciously (intentionally) or unconsciously (unintentionally). Under conscious assumption, one is aware of the risk to which hisher business is exposed, but essentially does nothing to avoid I I it. A manager of a business who consciously assumes risk is doing something about it by the very act of being aware of those perils and hazards which may cause loss. Being aware of risk, he may knowingly or unknowingly make adjustments in operations which will help to alleviate the impact of that risk. Awareness of risk itself is a significant achievement in better management. In the case of unconscious risk assumption, risk is not recognised. As you are not even aware of the existence of some risk, losses stemming from it can cause disastrous surprises to your business.

II) Loss Prevention: Another method of handling risk is to take appropriate measures to prevent the occurrence of a peril or minimise its financial impact on business. This approach is known as loss prevention. For example, by using fire resistant building material, you can prevent the occurrence of fire in the building. Loss prevention may not totally eliminate the risk, but can reduce its probability in terms of frequency as well as severity.

III) Avoidance: Avoiding situations which have the potential to cause loss, is another approach. For instance, a firm can avoid the risk of loss due to bad debts by simply stopping credit sales.

IV) Transfer: Transferring the risk to another party is a very widely followed approach to handle risks. Insurance is the most common method of transferring pure risks such as fire, windstorm, flood, riot, theft, etc. Business enterprises normally transfer the pure risks to the insurance company and devote their full efforts to their normal business.

V) Separation: Fifth method of risk control is separation of the firm's exposers to loss instead of concentrating them at one location where all of them might be involved in the same loss. For example, when a firm keeps its entire raw material in one warehouse, the entire raw material may be damaged if fire occur in that warehouse. Therefore, the firm may decide to store the raw material in ten separate warehouses. If fire occur in one warehouse, materials stored in that warehouse are damaged and the remaining nine warehouses are safe. This methods is also a kind of loss prevention.

VI) Combination: Strategies like diversification of products, law of large numbers, formation of more companies with unrelated lines of business, etc., come under this method. For example, if a firm is engaged in more products, the losses incurred in one product may be upset by the gains in another product. Similarly, if there are more companies, the losses incurred by one company may be upset by

the gains by the other companies. Insurance companies work on this combination principle where a sufficiently large number of similar objects are combined to make the loss predictable within narrow limits.

While managing risks, one need not just rely on any one method, instead may rely on some combination of various methods.

iv)After taking a decision regarding the combination of risk management tools, the next step is the implementation of the decision made. For instance, if you have decided in the previous stage to transfer the risk, you have to get the insurance policy at this stage.

v) Last step is to evaluate the effectiveness of the risk management tools we have implemented.

The result of the decisions made in the four stages must be evaluated to determine their effectiveness and change the strategy, if required.

5. What is a public utility ? Explain its features. (3+7)

Ans: Water, gas, electricity, transport communication, etc.,, are needed by the public in their daily life. Whenever there is any interruption in the supply of such goods or services, the normal life of people is disturbed. For example, If the electricity supply or transport services are not available, public life and activities are severely upset. these services have a great significance to the community. Hence they are termed as essential services or indispensable necessities. The business enterprises established basically to provide efficient and uninterrupted supply of the goods that are absolutely indispensable for a civilised community are referred to as public utility organisations.

Public utilities are the business undertakings engaged in supplying essential goods and/or services of daily necessity for the general public. The institutions which undertake certain essential services like the Supply of gas, water, electricity, urban transport, etc., are examples of public utility undertakings. All the public utility undertakings have an obligation to supply the essential goods and services to everyone in the community without any discrimination at reasonable prices.

Features of the public utilities are:

1) Indispensability: Public utilities deal with essential services such as water, gas, light, power, transport, telephone, telegraph, postal services, etc. These services are required to meet basic needs of the community and to provide a civilised and comfortable life to every citizen irrespective of caste and creed. Therefore, these services must be made available regularly, uniformly and adequately. That is why these public utilities are indispensable in all modem societies.

2) Field of operation: The field of operation of public utility undertakings is mostly local. Such concerns fulfil the needs of the citizens, usually of a city, town or at the most of a district. Fo; example, Delhi Milk Supply Undertaking or Mother Dairy supplies milk through its booths at various localities to the people living in Delhi only.

3) Monopolistic or semi-monopolistic position: Undertakings supplying essential public services by nature assume the position of a monopoly. They do not have competitors. You can take the example of Delhi Electric Supply Company. It does not have any competitors for supplying electricity to the residents of Delhi. If another undertaking is involved in the same operation in the same town, equal

amount of money is required which is a waste. To avoid any such wasteful expenditure, monopoly is given to public utilities. However, some public utilities may have a few competitors. Take the case of milk supply in Delhi. Mother Dairy supplies the milk. But Delhi Milk Supply Undertaking or Nanak Milk Supply Company also supplies milk in Delhi. Therefore the position enjoyed by Mother Dairy is semimonopolistic.

4) Regulation and control : These undertakings enjoy a monopolistic or semi-monopolistic position. So, they are in a position to misuse it and exploit the customers. For instance they may supply poor quality goods, services may be irregular, may charge high prices, etc. The government has to ensure the quality of the products or services at reasonable prices. Public is to be assured of regular and adequate supply of services and goods without discrimination. Therefore, it is essential to regulate their working as well as the price and supply policies of public utilities. Regulatory powers of the government in respect of these undertakings are provided in Special Acts of the legislature.

5) Franchise: Public utilities operate under franchise i.e. the right to interfere with public property (land, buildings, roads, etc.) for proper functioning. For example, the railways which is a public utility undertaking, can put up barriers on roads restricting movement of traffic across railway track at level crossings. Similarly, water supply undertakings can dig pits across the roads while laying water pipes, and so on. The government grants special rights as well as casts duties and responsibilities on these concerns through a charter which is called franchise. The franchise or charter contains the powers, privileges and rights granted to these undertakings as well as duties and liabilities for which these undertakings are accountable. This is done to ensure their working efficiently and satisfactorily. The franchise can be withdrawn if the undertaking does not comply with the regulations and resttictions subject to which the franchise is issued.

6) Huge capital investment: These undertakings require huge capital investment in fixed assets. Take the case of Mother Dairy which supplies milk in Delhi. For supply of milk . to its consumers it has to set up a milk plant, storage plant, and large fleet of vans1 tankers. It has also to construct depots for distribution of milk at various places in different localities of Delhi. Then, it has to monitor the distribution of milk to its consumers properly. Thus, all the public utilities invest huge amount of capital in fixed assets.

7) Risk involved: The degree of risk involved in the business carried out by the public utilities is less as compared with other industries. This is because the demand for essential goods and services is not likely to fall, rather it is likely to increase over time. For instance, the demand for water, gas, milk, electricity, etc., is not likely to fall but increase since the population is increasing continuously year after year.

8) Non-transferable demand by the consumer: The demand of the consumer is nontransferable. If a consumer is provided electricity at his house, he cannot transfer his right of using electricity to his neighbour. Every consumer is to obtain the supply separately after fulfilling the rules and regulations of the undertakings.

9) Choice of site: The promoters of public utilities do not have much choice in the selection of site for the undertaking. They have to locate their enterprise as per the permission granted to them by the concerned authorities. They have to operate as per . the prescribed local conditions and regulations.

10) Size of the undertaking: These undertakings are required to be set up on a sufficiently large scale so as to meet the demand of the public of that locality. Moreover, the size of the unit must be large enough to make it possible for the undertakings to supply the service continuously at economical rates.

6. Outline the factors which influence the choice of distribution channel. (10)

Ans: The following factors generally influence the choice of distribution channel:

1) Distribution policy

2)Characteristics of the product

3) The target customers in view

4)Supply characteristics

5)Types of middlemen in the field

6) Channel competition

7) Potential volume of sales

8) Costs of distribution

9) Profits expected in the long-run

1)Distribution policy: Where the manufacturer is interested in distributing his products through all possible outlets, it is desirable to use more than one channel to reach the target customers. This is known as intensive distribution policy. The purpose in this case is to make the product available as near to the consumers as possible. Consumer goods of frequent use like pens, pencils, paper, soap, hair nil, etc., are distributed through a large number of wholesalers and retail traders. If goods are meant for customers who are very particular about their quality and usefulness, manufacturers adopt a selective distribution policy.

2)Characteristics of the product: The nature of the product influences the choice of channel. For example, perishable products like eggs, milk, etc., are supplied either directly or through the short channels. In the case of heavy and bulky products (e.g., cement, steel) where distribution and handling costs are higher, short channels are preferred. Sophisticated electrical and electronics equipment which require careful handling are also generally distributed directly or through short channels. On the other hand, long channels are found in the case of light-weight and small-size items like dress material, readymade garments, pocket calculators, stationery, toothpaste, toothbrush, etc. Similarly, simple mechanical products like electronic toys, time-clocks, etc., are supplied through long channels for intensive distribution.

3)Characteristics of target customers; If the number of customers is large and geographical area is extensive, long and multiple channels are necessary for intensive distribution of goods. This is also suitable where the consumers are in the habit of making frequent purchases of small quantities at irregular intervals. Short channels and direct selling are possible in the case of few customers who purchase large quantities at regular intervals and they are concentrated in a small area.

4)Supply characteristics: Goods produced by a small number of producers concentrated in one region are generally distributed through short channels. Long channels are suitable if a large number of producers in different regions produce and supply the goods.

5)Types of middlemen: Availability of suitable middlemen in the channel of distribution is another factor in the selection of the channel. This is because different functions like standardisation, grading, packing, branding, storage, after sale servicing, etc., are expected to be performed by middlemen. Efficiency of distribution depends upon the size, location and financial position of middlemen. If the middlemen in a specific channel are dependable and efficient that channel may be preferred by producers.

6)Channel competition: There are different situations in which manufacturers compete with each other for availing the services of particular wholesalers. Similarly, wholesalers often compete with each other to deal with particular retailers or carrying particular brands of products. Sometimes producers use the same channel which is used by their competing producers. If any producer arranges exclusive distribution through a particular wholesaler, other producers also do the same. Thus, selection of a channel may depend on the competition prevailing in the distribution system.

7)Potential volume of sales: The choice of the channel depends upon the target volume of business. The ability to reach target customers and the volume of sales varies between different channels. One outlet may not be adequate for achieving the target in which case more channels need to be used. Of course, the competitive situation must be taken into account while examining the potential volume of sale through different channels.

8)Cost of distribution: The various functions carried out in the channel of distribution add to the cost of distribution. While choosing a channel, the distribution costs of each channel should be calculated and its impact on the consumer price should be analysed. A channel which is less expensive is normally preferred. Sometimes, a channel which is convenient to the customers is preferred even if it is more expensive. In such cases the choice is based on the convenience of the customers rather than the cost of distribution.

9)Long-run effect on profit: Direct distribution, short channels, and long channels have different implications with regard to the profits in the short-run and long-run. If demand for a product is high, reaching the maximum number of customers through more than one channel may be profitable. But the demand may decline in course of time if competing products appear in the market. It may not be economical then to use long channels. So, while choosing a channel one should keep in mind the future market implications as well.

7. Discuss various methods of raising short-term capital. [10]

Ans: The following methods may be used to raise short-term capital:

1) Trade credit

2) Factoring

3) Discounting bills of exchange

4) Bank overdraft and cash credit

5) Public deposits

1)Trade credit: Just as companies sell goods on credit, they also buy raw materials, components, stores and spare parts on credit from different suppliers. Hence, outstanding amounts payable to trade creditors as well as bills payable relating to credit purchases are regarded as sources of finance. Generally, suppliers grant credit for a period of 3 to 6 months, and thus provide short-term finance to the company. Availability of this type of finance is closely connected with the volume of business.

When the production and sale of goods increase, there is automatic increase in the volume of purchases, and more of trade credit is available. On the other hand, if sales decline there-is a corresponding decline in purchases of materials, and consequent decline in trade credit as a source of finance. Thus, creditors' balances (accounts payable) and bills payable help companies to finance current assets, i.e., stock of materials and finished goods as well as book debts. However, trade credit also involves loss of cash discount which could be earned if payments were made within 7 to 10 days from the date of purchase. This loss is regarded as the cost of trade credit.

2)Factoring: The amounts due to a company from customers on account of credit sale generally remain outstanding during the period of credit allowed i.e., till the dues are collected from the debtors. By this arrangement the responsibility of collecting the debtors' balances is taken over by the bank on payment of specified charges by the company. This is a method of raising short-term capital and known as 'factoring'. It helps companies to secure finance against debtors' balances before the debts are due for realization, and incidentally also helps in saving the effort of collecting the book debts. The disadvantage of factoring is that customers who are in genuine difficulty do not get the facility of delaying payment which they might have otherwise got from the company.

3)Discounting bills of exchange: Discounting of a bill of exchange is a method of short-term financing provided by banks. When goods are sold on credit, bills of exchange are generally drawn for acceptance by the buyers of goods. The bills so drawn are payable after 3 or 6 months depending on the prevailing practice among traders. Discounting of the bill refers to the encashment of the bill before the date of its maturity. Instead of holding the bills till the date of maturity, companies generally prefer to discount them with commercial banks on payment of a charge known as bank discount. This process of encashing the bill with the bank is called discounting the bill. Bills are endorsed in favour of the bank so that the bank gets the amount from the drawee on the due date. The amount of discount is deducted from the value of bills at the time of discounting. The rate of discount to be charged by banks is prescribed by the Reserve Bank of India from time to time. It really amounts to the interest for the period from the date of discounting to the date of maturity of the bill. If any bill is dishonoured on maturity, the bank returns it to the company which then becomes liable to pay the amount to the bank. The cost of raising finance by this method is the discount charged by the bank.

4) Bank overdraft and cash credit: Cash credit refers to an arrangement on a continuing basis whereby the commercial bank allows money to be drawn as advance from time to time within a specified limit known as cash credit limit. This facility is granted against the security of goods in stock, or promissory notes bearing a second signature, or other marketable instruments like Government bonds. The company is allowed to draw whatever amount is required at different times within the limit agreed upon. The cash credit limit may be revised according to the value of securities. The money drawn can be repaid as and when possible. Interest is charged on the actual amount withdrawn. It is offered for maintaining the working capital of the business. The loan duration is generally 1 year. An overdraft is a temporary arrangement with the bank which permits the company to overdraw from its current deposit

account with the bank up to a certain limit. The overdraft facility is also granted against securities as in the case of cash credit. Interest is charged only on the amount actually overdrawn. Overdraft facility is offered for meeting short-term obligations of individuals or businesses. The loan duration can vary and it can be monthly, quarterly, half yearly or yearly.

5) Public Deposits: Companies often find it convenient and necessary to raise funds by inviting their . shareholders, employees and the general The Companies Act permits such deposits to be received for a period up to 3 years at a time. Thus, public deposits can be raised by companies to meet their shortterm and medium-term financial needs. It is a simple method of raising finance for which the company has only to advertise in the newspapers giving particulars about its financial position as prescribed by the Companies Act. The deposits are not required to be covered by mortgaging assets or by other securities. Moreover deposits can be invited by offering a higher rate of interest than the interest on bank deposits. C public to deposit their savings with the company. But companies are not permitted to raise unlimited amounts of fund through public deposits.

8. Explain the relationship between a banker and its customer. [10]

Ans: The relationship between a banker and a customer is as follows:

i. Contractual Relationship: The primary relationship between a banker and a customer arises from a contract between the two, so it is a contractual relationship. The contract takes place the moment an account is opened by a customer with a bank and this contract remains valid till the customer operates his account as per the terms and conditions agreed between them.

ii. Debtor and Creditor Relationship: The relation of a banker and customer is primarily that of a debtor and creditor. When a customer opens an account with a bank and maintains e credit balance, the banker assumes the position of a debtor and the customer assumes the role of a creditor. Money deposited with the bank becomes a debt due from him to the customer. The banker can use the money deposited with him by the customers in any manner according to his discretion, his only obligation being to repay the debt as and when demanded by the customer.

iii. Bailee and Bailor Relationship: When a bank accepts deposits of money, he does not act as a bailee. This is so because a bailee accepts the bailment of goods on the condition that the things bailed will not be utilised by him and the identical goods will be returned. But a bank does not accept money from customer on the condition that it will not utilise the money and that the identical money (the same currency notes or coins deposited by customer) will be returned. A banker provides for safe deposit vaults and accepts documents and valuables for safe custody. Here the bank is acting as a bailee and the relationship is that of bailee and bailor.

iv. Trustee Beneficiary Relationship: Banks also act as trustees and executors of will of customers. A trustee is required to hold property and money and use the trust money in accordance with the trust deed and use it for the benefit of some other person known as beneficiary. A customer may deposit some money with the bank for a specific purpose with specific instructions to the bank regarding its use. In such cases, the banker is the trustee of the customer's money, and the banker cannot employ them for any other purpose other than the purpose specified by the customer. The legal position of a banker as a trustee is different from that of a debtor to the customer. The relationship is determined by the particular circumstances in each case. For instance, when a bank receives a cheque from the customer

for collection from another bank, the bank becomes a trustee till the amount of cheque is realised. Once the amount is credited to the customer's account, the banker assumes the position of a debtor.

v. Principal-Agent Relationship: Banks perform many agency functions such as collection of cheques or drafts or bills, collection of interest and dividends on securities, arranging for remittances and payment of insurance premiums, etc., as per the instructions of the customers. In all such cases, the bank is acting as an agent of the customer. In these cases the position of a customer is that of the principal and the position of the banker is that of the agent. Here the bank has to act according to the instructions of the customer.