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ECO-01 Business Organisation

1. What do you understand by Business Organization ? What are the basic forms of Business Organisation ? 2+8

Ans: Business is an economic activity concerned with the production or purchase and sale of merchandise and rendering of services with the purpose of earning profit. The primary objective of a business is to earn profit. A business can be established by the decision of the entrepreneur and fulfilling certain legal formalities. Any person can start a business, there is no minimum qualification to run a venture. It requires capital investment according to its size and nature. A business gets profit as a return for the work done by him/her. Transfer of interest is common. By following required legal formalities, business can be transferred to others. Risk factor is always present in business. There is risk of loss. Every business advertises its products and services, for the purpose of increasing sales. A business activity becomes a reality only when efforts are,made to bring the required resources together, put them at work systematically, and coordinate their activities properly. This is referred to as business organisation.

Another definition for organisation is a combination of necessary beings, materials, tools, equipment, working space apparatus and finance brought together in a systematic and effective correlation to accomplish some desired objective.

Another definition is " the process of combining the work which individuals and groups have to perform with the facilities necessary for its execution so that they provide the best channels for efficient, systematic, positive and coordinated application of the available effort".

The four different forms of organisation are: i) Sole trader organisation ii) Partnership form of organisation iii) Company form of organisation iv) Cooperative form of organisation

i)The sole trader organisation (also called proprietorship) is the oldest form of organisation and the most common form of organisation for small business even today.

It is the simplest and easiest to form.

The main features of sole trader organisation is as follows:

i) One man ownership: The ownership lies with one person only. There are no associates or partners. He invests his own money or borrows from friends and relatives.

ii) No separation of ownership and management: The owner himself manages the business. Therefore, the separation of ownership and management which is quite common in big business is not present in this form of organisation. Since the proprietor himself manages the business, he exercises a high degree of supervision and control in the working of his business.

iii) No separate entity: The business does not have an entity separate from the owner. The proprietor and the business enterprise are one and the same.

iv) All profits to proprietor: Since there are no partners, all the profits are enjoyed by the sole proprietor.

v) Individual risk: All losses in the business are borne by the proprietor himself.

vi) Unlimited liability: The proprietor has an unlimited liability. This means that in case of loss even the personal property of the owner can be utilised for clearing the business obligations and debts,

vii) Less legal formalities: To set up sole proprietorship, no legal formalities are required. There are some legal restrictions for the setting up of a particular type of business.

ii) Partnership form of organisation: A partnership is a form of business organisation in which two or more persons upto a maximum of twenty join together to undertake some form of business activity".

The persons who own the partnership business are individually called 'partners' and collectively known as the 'firm’ or 'partnership firm'. On an agreed basis, partners contribute to capital and share the responsibility of running the business.

Different partners play different roles in the operations of the firm. One partner may contribute more capital while another partner may spend more time in managing it. Depending on the role played, we can classify the partners into various categories.

Based on the extent of participation in the functioning of the business, we can classify partners into:

(a) active partners, and

(b) sleeping partners.

a) Active partner: If a partner takes an active part in the management of the business, we call him as active partner. He is also known as a 'working partner'.

b) Sleeping partner: If the partner is not actively associated with the working of the partnership firm, we call him a sleeping partner. A sleeping business partner simply invests his capital. He does not participate in the functioning of the firm. Such a partner is also known as a 'dormant partner'.

Based on the sharing of profits, partners may be classified into:

(a) nominal partners, and - (b) partner in profits.

a) Nominal partner: A partner who just lends his name to the partnership is known as a nominal partner. He neither invests his capital nor participates in the day-to-day working Business Organisation and management of the firm. Such partners are not entitled to a share of profits, but they are liable to other parties for all the acts of the firm.

b) Partner in profits: A partner who shares the profits of the business without being liable for losses is called a partner in profits. As a rule, he will not take any part in the management of the business.

Based on the behaviour and conduct exhibited, the partners may be divided into: (a) partner by estoppel, and (b) partner by holding out.

a) Partner by estoppel: A person who behaves in the public in such a fashion as to give an impression that he is one of the partners in a partnership firm is called a partner by estoppel. Such partners are not entitled to profits but are fully liable as regards the firms obligations.

b) Partners by holding out: If a particular partner of a firm represents that another person is also a partner of the firm, and if such a person does not disclaim the partnership relationship even after coming to know about it, such person is called a 'partner by holding out'. Such partners are not entitled to profits but are liable as regards the obligations of the firm.

main features of partnership form of organisation are:

i) PIurality of persons; To form a partnership firm, there should-be at least two persons.. The maximum limit on the number of persons is ten for banking business and twenty for other types of business.

ii) Restriction on transfer of share: A partner cannot transfer his share to an outsider without the consent of all the other partners.

iii) Profit sharing: There must be an agreement among the partners to share the profits and losses of the business of the partnership firm. This is one of the basic elements of partnership. If two or more persons jointly own some property and share its income, it is not regarded as partnership.

iii) Company form of organisation:

Features of company form of organisation are as follows:

Incorporation: A company is an incorporated association. It comes into existence only after registration under the Companies Act.

Artificial person: A company is regarded as an artificial person as it is created by law and can be effaced only by law. It has no body, no soul, no conscience, still it is in a position to exist. Like any other person it can own property, conduct a lawful business, enter into contracts with others, buy, sell and hold property, all under its own name and its own seal.

Common seal: As the company is not a natural person, it cannot sign the documents. It has a device in the form of common seal on which its name is engraved. This common seal is a substitute of its signatures. It is affixed on all important legal documents and contracts.

Separate Legal Entity: A company has a distinct entity and is independent of its members or people controlling it. A separate legal entity means that only the company is responsible to repay creditors and to get sued for its deeds. The individual members cannot be sued for actions performed by the company. Similarly, the company is not liable to pay personal debts of the members.

Perpetual Existence: A joint stock company has a continuous existence. Unlike other non-registered business entities, a company is a stable business organisation. Its life doesn’t depend on the life of its shareholders, directors, or employees. Members may come and go but the company goes on forever.

Number of members: In the case of a public limited company: the minimum number is seven and there is no maximum limit. In the case of a private limited company, minimum number is two and the maximum is fifty.

Limited liability: The liability of the members of a company is normally limited by guarantee or by the shares. Members liability is limited to the amount of shares held. Members are not personally liable for the debts of the company. So, personal properties of the members are not liable to be attached for the payment of the company's debts.

Transferability of shares: In public limited company, members have the rights to sell his shares to others without the consent of other shareholders. However, there are restrictions for transferring shares in case of a private limited company

iv) Cooperative organisation: 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.

2. What do you understand by Sole Trader Organisation ? State the merits and limitations of Sole Trader Organisation. 2+8

Ans: The sole trader organisation (also called proprietorship) is the oldest form of organisation and the most common form of organisation for small business even today.

It is the simplest and easiest to form.

Sole trader organisation as "one man's business in which an individual produces independently with his own capital, skill and intelligence and is entitled to receive all the profits and assumes all the risks of ownership". J.L. Hanson defines it as "a type of business unit where one person is solely responsible for providing the capital for bearing the risk of the enterprise and for the management of the business".

Merits:

1. Easy formation: There are no legal formalities to be observed while starting this form of organisation. Therefore, its formation is very easy and simple. The expenditure involved in the process of formation is also negligible.

2. Direct motivation: As you know, all the profits and gains of the business are solely and exclusively pocketed by Lhe sole proprietor. This motivates the proprietor to work hard and develop the business to get more and more profits. His involvement in the business is, therefore, complete and free.

3. Full control: The proprietor is the monarch of the business he owns. He manages the whole business and takes all decisions himself. In other words, proprietor exercises full control over the functioning and working of the business.

4. Quick decision: The proprietor does no1 depend on others for decision making. Since there are no partners, he is not required to consult others. This enables the proprietor to take quick decisions on nunlerous matters concerning his business.

5. Flexibility in operations: Being a small organisation it is easy to bring changes if situation so demands. In a large sized organisation to bring changes is difficult.

6. Secrecy: Since the whole business is handled by the proprietor his business secrets are known to him only. He is not bound to publish his accounts. Therefore, the degree of secrecy is the highest in this form of organisation.

7. Personal touch: When the proprietor handles everything relating to the business himself, it is easy to maintain a personal rapport with the customers. He can easily know their tastes, likes and dislikes and adjust his operations accordingly. Similarly, in this form of organisation, employees, if any, work directly under the proprietor. So, it gives scope for the proprietor to maintain harmonious relations with the employees.

8. Dissolution easy: Since there are no co-owners or partners, there is no scope for the difference of opinion in the case of dissollltion of business. The proprietor is free to withdraw from the business or to sell it at any time he wants. Because of ease in formation and withdrawal, proprietorship form is often used to test business ideas.

Limitations:

1. Limited resources: The capilal and other resources of an individual are always limited. The sole trader has to mainly rely on his own money and earnings, or he can borrow, if necessary, from relatives and friends. Thus, the proprietor has a limited capacity to raise funds. This makes it difficult to plan any large scale expansion.

2. Limited managerial capability: In the modern business, knowledge and skills in various fields like production, finance, marketing, etc., are required. It is not possible for a single individual to possess expertise in all these areas. So, his decisions may not be balanced.

3. Not suitable for large scale operation: Sincathe resources of the sole trader are limited, it is suitable only for small business and not for large scale operations.

4. Unlimited liability: You know that the proprietor has an unlimited liability. In case of a loss, eveh his personal property and belongings can be utilised for clearing business obligations. Therefore, he cannot take much risk and is discouraged from expansion of his business.

5. Less stability: The continuity and stability of the business depends solely on one person. When the man dies, there is a likelihood of closure of the business.

6. No check and control: As the sole trader is the monarch of the business, no outsider can question him on his acts and deals. There are no checks and controls on the sole trader.

7. Less scope for economies of scale: Sole trader usually operates on small scale only. So, he can not enjoy the benefits of large scale production or buying or selling. This may raise the cost of business operations.

3. Compare the relative advantages and disadvantages of issuing equity shares and preference shares. 10

Ans: Equity shares: There are several advantages of issuing equity shares to raise ownership capital. The rate of dividend on these shares depends on profits available and the discretion of directors. There is,

therefore, no fixed burden on the company. The shareholders expect high rates of dividend ingrofitable years. But they also bear the risk associated with uncertainty of earnings of the company. Thus, risk capital is available by issuing these shares. Further, the amount raised by issue of equity shares can be used permanently. It is not required to be paid back so long as the company exists. Moreover, equity shares do not require mortgaging of the company's assets. Additional funds can be raised as loan on the security of assets.

However, excessive issue of equity shares may create problems for the promoters who may like to control the management of the company. Each equity share carries one vote for the holder. So holders of equity shares may form groups and vote against the existing directors of the company. This may not be always in the best interest of the company as a whole. Secondly exclusive dependence on equity share capital may not permit the company to take advantage of trading on equity. Besides, once equity shares are issued the amount become a permanent capital which at times may be more than what the company can use profitably. In that case, there is no way of reducing it unless detailed legal formalities are complied with. Also reduction of share capital damages the image of the company.

Preference shares: Issue of preference shares is another method of raising long -term capital. It has certain merits. Dividend is payable on preference shares at a fixed rate and is payable only if there are profits. Hence, there is no compulsory burden on the company's finances. Secondly, preference shareholders do not have voting right. So they cannot take part in the management of the company and thus are not a threat' to the promoters. Another advantage of preference shares is that the company can declare higher rates of dividend for equity shareholders in good years because the rate of preference dividend is fixed. Besides, permanent use of preference share capital is also not essential. A company may issue redeemable preference shares and have the flexibility of paying off the amount if necessary and replace it by some other type of capital.

Sonie investors subscribe to preference shares because of preferential rights as to the payment of dividend 'and the return of capital. But others do not prefer it due to the fixed return as well as some risk of non -payment of dividend. Also they do not derive any benefit by way of rise in market price of the shares as is the case with equity shares.

4. “Foreign trade is an engine of economic growth in a country.” Discuss this statement. 10

Ans: Importance of foreign trade in economic development of a country:

i) Specialisation and efficiency of production: Foreign trade leads to specialisaiton in productive activities undertaken by different countries. Depending on available natural resources, and development of science and technology, every country can produce only those goods and services for which it has the greatest relative advantage and efficiency. No country has facility and resources within its own boundaries for economical production of all its requirements: Some countries are more suitably placed to produce certain goods/services economically and sufficiently than other countries. Therefore, they can specialise in the production of such goods and get the goods they need in exchange for those goods, For example, India has comparatively greater advantages for the production of agrobased products such as coffee, tea, sugar, textiles, etc. Similarly some developed countries such as USA, Japan, Britain, etc. have greater advantages for the production of industrial machinery, automobiles etc. Some gulf countries such as Iran, Libya, Iraq, Saudi Arabia, etc. produce crude oil, petroleum, etc., in abundance.

ii) Facilitates economic development: Rapid economic development and growth of national income can be facilitated on the basis of exports and imports. Indeed, it is on the basis of imports of raw materials and export of manufactured goods that countries like U.K., Japan etc., have achieved a high rate of economic growth.

iii) Equalisation of prices: International trade equalises prices of goods throughout the world. Whenever the prices of commodities tend to rise in a country, it can increase the level, of its imports to check the rise in prices. Similarly, whenever prices of products decline, the trend may be counteracted by exporting the same.

iv) Employment opportunities: Foreign trade facilitates the growth of agricultural as well as industrial activities which in turn generates more employment in the country.

v) Harmonious relationship between countries: Because of foreign trade every country may have access to goods that it does not produce at home. Similarly, a country with a surplus of certain goods can make them available to other countries experiencing shortage of those goods. This promotes harmonious and cordial relationship among various countries.

vi) Utilisation of resources: Every country possesses some natural resources. The economic development of a country heavily depends upon exploitation of these resources. For example, India has adequate offshore oil resources. But, it requires exploitation through sophisticated machines, technology, etc. which we do not h8ve. Machinery and technology can be imported from the developed countries like USSR, USA, Japan, etc. This leads to best possible use of natural resources.

5. What is Bank ? Discuss the types of accounts in a Bank. 2+8

Ans: Bank is an institution which deals in money. Banks accept surplus money from those who are not needing it immediately and lend it to those who need it. An institution which accepts deposits from public repayable on demand and invests or lends the money. It also provides various other services to its customers. Banks may be commercial banks, co-operative banks, Land Development Banks, Rural Banks, Industrial Banks and Central Bank.

Banks play a very important role in the economic development of the country. They encourage habit of savings among people. We can make payments easily and safely through banks. Banks provide different types of credit facilities to its customers. Money can be remitted to at far of places with the help of banks.

The main type of accounts in a bank are fixed deposit account and recurring account (for time deposits), savings bank account and current account (for demand deposits).

Fixed Deposit Account: The fixed deposits are the most popular form of deposits raised for the banks. This type of account is most suitable for persons who have spare money to invest for long duration but do not want to invest in risky securities. The term 'fixed deposit' means the money or deposit is made for a fixed period of time at a fixed rate of interest. This period may vary from forty five days to several years. This period is decided by the customer according to his convenience. The rate of interest is usually higher than other types of deposits, because the bank knows that the deposit money is repayable only after a certain period. The rate of interest on fixed deposit depends on the period of deposit, the longer

is the period of deposit, the higher will be the interest fate. The interest rate is decided by the Reserve Bank of India from time to time and all banks have to follow that rate structure.

Current Account: Current accounts are intended for businessmen, joint stock companies, public institutions, etc., whose banking transactions happen to be numerous on every working day. A current account is a running and active account which may be operated upon any number of times during a working day. There is no restriction on the number and the amount of deposits or withdrawals from this account. Since the amount from this account is repayable on demand, the banks are required to keep sufficient cash to meet such demands. Therefore, the banks pay no interest on current account deposits. The banks charge incidental charges on an unremunerative current account for the work and expenses involved in its maintenance. The main advantage of current account is that the customers are relieved from the botheration of handling cash. Third party cheques with endorsements can be deposited in the current account for collection and credit to customer's account. Overdraft facilities are given in this type of account and loans and advances are granted by the bank.

Savings Bank Account: A savings bank account is opened and operated by people who wish to save a part of their income for his future needs and also earn some interest on his deposits. This type of account is intended to promote the habit of saving among depositors, therefore, some restrictions have been imposed on the number and the amount of withdrawals from this account.

Recurring Deposit Account: Recurring deposit accounts are meant for people who have regular monthly incomes. This type of account is intended to encourage the habit of savings among depositors on a regular basis. In this account, the depositor deposits a fixed sum of money every month for an agreed period and at the end of the specified period, he gets back the amount deposited together with the interest accrued thereon. The period for which a recurring account is opened varies from one year to ten years. The rate of interest is higher than in a savings bank account. The pass book is to be presented to the bank every month when a deposit is made, so as to enable the bank to record the deposit therein.

6. What is Public Utility Undertaking ? State its essential characteristics. 2+8

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.

Characteristics of 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 whiIe 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.

7. Discuss instruments of government control on private business. 10

Ans: Government regulation of private business does not necessarily mean only restriction of private activities. As a matter of fact government measures of control may have inducive as well as restraining effects on business. Measures may have inducive effects if the objective is to stimulate, encourage, facilitate or induce a particular type of trade or industrial activity through technical and financial assistance, tax concessions, subsidy, bank credit, supply of foreign exchange for imports of raw materials or machinery, protection against foreign competition, etc. On the other hand, certain measures may have restraining effects if they are aimed at limiting or restricting private trade and industry by means of legal enactment and administrative orders. These may include licensing requirements for starting or expanding industries, control over capital issues, fixation of maximum price, etc. However, some of the measures may have both the effects. For example, industries which require imported raw materials may be adversely affected if imports of such raw materials are restricted or stopped. At the same time, due to such restriction on imports, the producers of competing goods may have a positive effect and earn more profit. There is another way of distinguishing between the instruments of control. Thus, controls may be classified into two categories depending on whether the measures are directly applicable or indirectly applicable. Accordingly, the two broad types of control measures may be: 1) direct controls and 2) indirect controls.

Direct Controls: Direct controls are the measures which are applied at the discretion of government authorities. Such a control may be used to promote. restrict or limit the activities of private organisations or categories thereof. Examples of these controls are:

1) Licensing of new enterprises or expansion of existing large enterprises. 2) Control over issue of shares, debentures, etc., by companies for raising capital (control of capital issues). 3) Import and export control through direct prohibition or quota restriction. 4) Fixing maximum or minimum prices for particular commodities. 5) Control over distribution of commodities through rationing. 6) Grant of subsidies for industrial growth. 7) Incentives for export promotion like grant of subsidy, credit facilities, etc.

These controls are also knows as discretionary controls because they involve discretions to be made by concerned government officials.

Indirect Controls: These indirect controls affect private business firms in an indirect manner. The following are some common examples of indirect controls:

1) Changes of tax rates: Tax rates may be lowered to encourage the business or raised to discourage the business.

2) Changes in import and export duties: Import duties may be raised so as to increase the prices of certain goods. This may be aimed at discouraging imports of those goods or to protect domestic industries from foreign competition. Import duties may be lowered to allow large imports of certain products. Similarly, export duties may be raised or lowered so as to influence the domestic demand and supply. For instance, if the export duty is raised, exports may be discouraged and domestic supply may increase to meet higher domestic demand. If it is lowered, exports may rise.

3) Changes in interest rates on bank loans: Government can change its monetary policy to control the prices. For instance, interest rates on bank loans and credit may be raised so as to prevent excessive borrowing and expenditure by business enterprises and to reduce new investment by business firms. On the other hand, interest rates on bank loans may be reduced to induce business firms to borrow and expand their business activities, Indirect controls are also known as non-discretionary controls. Government authorities do not have any discretionary power to apply the measures to particular firms and not to others in the same category.

Economic Planning:

Many developing countries today have recognised the importance of planning for economic development and adopted broad economic policies for industrial growth. In India this is done through Five Year Plans. The First Five Year Plan was launched in 195 1. Since then, six successive plans have been completed and the Seventh Five Year Plan is running its last year. The main objectives laid down in the plans have been:

i) To achieve a target growth of national income so as to improve the standard of living of people.

ii)To bring about industrial growth according to certain priorities and with particular emphasis on basic and heavy industries like steel, fuel and power, chemicals, fertilisers, engineering goods, etc., and provision of transport and communication facilities.

iii) To generate more employment opportunities to absorb the increasing labour force.

iv)To increase agricultural production and achieve self sufficiency in foodgrains.

v) To reduce regional inequalities and achieve balanced regional development.

vi) For the utilisation of limited resources to the best possible advantage.

Economic planning gives a general indication of the priorities of development of various industries and accordingly guides the development process. Besides, it indicates the extent to which private organisations will be allotted scarce resources like fuel, power, finance and other facilities for growth. The economic and social activities which the government will undertake on its own are also laid down in the five year plans.

Industrial Policy The industrial development of our country is guided, regulated, controlled and promoted according to the industrial policy. After Independence, a number of policy statements have been issued by the Government of India which define the respective roles of government, private, cooperative and joint sector organisations in industrial development. Policies also indicate the relative importance of large, medium and small-scale industrial units. In April 1948, the government adopted the first Industrial Policy Resolution, which emphasised a progressively active role of the state in industrial development. At the same time, the policy also laid down that private organisations should play a complementary role within the framework of the policy.

In 1956 the government adopted a new industrial policy resolution with the following objectives.

i) To increase the rate of economic growth.

ii) To speed up industrial development.

iii) To enhance the scope of government participation in industrial growth.

iv) To prevent private monopoly and concentration of economic power.

V) To define the role of small, village and cottage industries.

vi) To bring about a balanced regional development.

Industrial Licensing

As an instrument of government control and regulation, the system of industrial licensing was introduced to implement the Industrial Policy Resolution. Provision was made for that purpose in the Industries (Development and Regulation) Act, 1951. The Act has provided that no n& industrial unit could be established or substantial expansion of existing plants made without a licence from the Central Government, Further, while granting licence for any new undertaking, govemment may lay down conditions regarding location, minimum size, etc..

The industrial licensing system was expected to achieve the following objectives:

1) Regulation of industrial development and guiding investment in industries according to the planned priorities and targets of growth.

2) To control monoply and concentration of wealth.

3) Protection of small-scale industries against undue competition from large units.

4) Prevention of concentration of industries in few locations and secure regional decentralisation of industries.

5) Best possible use of scarce foreign exchange resources.

8. Write short notes on any two of the following : (5+5)

(a) Types of Business Risk

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 the 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.

(b) Classification of Commerce

Ans: Commerce can be classified into two categories :

1) Trade-activities of purchase and sale.

2) Aids to Trade- activities which facilitate the smooth and uninterrupted flow of goods.

1) Trade-activities of purchase and sale.

The human activities engaged in buying and selling of goods and services come under trade. Therefore, trade includes sale, transfer or exchange of goods and services with the intention of earning profit. The objective of trade is to make goods available to those persons who need them and are willing to pay for them. 'Thus, trade plays 'a major role in establishing contact between the producers and the consumers and eliminates the hindrance of person.

A person who is engaged in trade is called 'trader' or 'middleman'. Various traders operate in between producers and consumers and remove the hindrance of person. We can classify trade into two broad categories: 1) internal trade, and 2) external trade.

1) Internal Trade: When the trade takes place within the boundaries of the country, you can call it 'internal trade'. It means that both buying and selling should take place within the country. Payment for the same is generally made in national currency. This internal trade is also termed as inland trade or national trade or home trade or domestic trade.

On the basis of the scale of operations, we can classify internal trade into: a) wholesale -trade, and b) retail trade.

a) Wholesale Trade: Buying and selling in relatively larger quantities is called wholesale trade. A person who is involved in wholesale trade is called wholesaler.

b) Retail Trade: This refers to buying and selling in relatively smaller quantities. A person engaged in retail trade is called a retailer.

2) External Trade: This is also called 'foreign trade' or 'internationnl trade'. When the trade takes place across the boundaries of a country, you can call such trade as external trade. In other words, external trade refers to the trade between nations. This trade could be in the form of exchange of one commodity for another or for money.

We can classify foreign trade into three categories:

a) import trade,

b) export trade, and

c) re-export trade.

a) Import Trade: when a country buys goods from another country, it is called 'import trade'. For example, India bought machinery from the USA. This is an import trade for India.

b) Export Trade: When a country sells goods to another country, it is called 'Export Trade'. For example, India sells leather goods to USSR, and tea to USA. For India such selling of goods shall be termed as 'export trade'.

c) Re-export Trade: This is also called 'entrepot trade', When the goods are imported from one country and the same are exported to another country, such trade is called 're-export trade'. Re-export is done by those countries which have ports that are conveniently situated to serve as distributing points for neighbouring countries. Such countries import large quantities of goods and re-export the same to the neighbouring countries.

2. Aids to Trade

Activities which facilitate the trade are called 'aids to trade'. Thus, all human activities which eliminate the hindrances and facilitate the flow of goods from producers to consumers come under aids to trade. They are also called 'auxiliaries to trade'. The whole range of activities coming under aids to trade may be classified into five categories: 1) transportation, 2) warehousing, 3) insurance, 4) advertising, and 5) banking.

1)Transportation: All the goods are not consumed at the same place where they are produced. In the modern times there is a vast distance between centers of production and the centers of consumption. Therefore, goods are to be moved from the place of production to the place where they are demanded. This difficulty is removed by an important aid to trade known as transport. Thus, transportation eliminates the hindrance of place and creates place utility to goods. Transportation can be of three types: a) Land transportation - road, rail b) Air transportation-aeroplane C) Water transportation-boat, ship

2) Warehousing: Warehousing is an act of carefully storing goods in warehouses to sell or distribute them later. Warehousing is essential because there is a time gap between production and consumption. In other words, goods which are produced at one time, are not consumed at the same time. Hence, it becomes necessary to make arrangements for storage or warehousing. Goods once produced should be preserved properly till they are consumed. Particularly, perishable goods like milk, meat, vegetables, flowers, etc., should be preserved very carefully. Otherwise, they get spoiled and become useless. For this reason warehousing is recognised as yet another aid to trade. Thus, warehousing eliminates the hindrance of time and provides time utility to goods.

3) Insurance: The goods may be destroyed while in production process, or in transit due to accidents, or in storage due to fire or theft, etc. The businessmen would like to cover thcse risks. Insurance companies come to their rescue in this regard. They undertake to compensate the loss suffered due to such risks. For this purpose, the business has to take an 'insurance policy' and pay a certain amount regularly, called 'premium'. Thus, insurance eliminates the hindrance of risk.

4) Advertising: Exchange of goods is possible only when the consumers have the knowledge about the existence of a product. This is the hindrance of knowledge. This hindrance is eliminated through advertising. Through advertisement, producers communicate all information about their goods to the prospective consumers and create in them a strong desire to buy the product. Thus, advertising facilitates the flow of goods between producers and consumers by bringing the knowledge about the products to the consumers. Advertising is done through TV, radio, newspapers, magazines, hoardings, wallposters, etc.

5) Banking: Banking solves the problem of finance. Banking facilitates the flaw of goods by removing the hindrance of finance and credit. Businessmen receive money and pays money in large amounts. It is

risky to carry a large amount of cash from one place to another. Here comes banking as a solution. Banking and financial institutions solve the problem of payment and facilitate a smooth exchange between buyer and seller. The businessmen may also require short-term and long-term funds. Bank provide such finance to businessmen. Banks also advance loans in the form of overdraft, cash-credit and discounting of bills of exchange etc.

(c) Kinds of Insurance

Various kinds of insurance are:

1)Life insurance

2)Marine insurance

3)Fire insurance

4)Motor insurance

5)Miscellaneous insurance

1)Life insurance: Life insurance is a contract under which one person, in consideration o fa premium paid (either in lump sum or by monthly, quarterly, half-yearly or yearly payment),undertakes to pay to the person for whose benefit the insurance is made, a certain sum of money either on the death of the person whose life is insured or on the expiry of a specified period of time.Life policies are considered as life assurance policies.The insurer must pay the agreed amount (policy amount) on the occurrence of the agreed event (death or expiry of the specified time).

Types of Life Policies: Some of the types types of life policies are discussed below:

Whole Life Policies: Under this policy, the sum assured is payable after the death of the assured. The premiums on whole life policies may be payable regularly through out the life of the assured, or alternatively they may be payable for a fured period only (say 20 or 30 years). If the premiums are paid throughout the life, it is called 'ordinary life policy'. In the other case when premiums are paid for a limited period, it is called 'limited payment life policy'.

Endowment Life Assurance: Under this policy the insurer undertakes to pay the sum assured either at the end of a specified period or on the death of the assured, whichever is the earlier. 1n case the assured dies before the expiry of specified period (or before attaining the specified age), the sum assured is payable to the legal heirs or nominees. If the insured survives till the policy matures (i.e, expiry of the specified period), the sum assured is paid to the insured himself. The premium for endowment policy is a bit higher than the whole life policy.

Term Assurance: This is also called temporary assurance. Under this policy, the sum assured is paid when the assured dies before the stipulated date. No payment is made if the assured survives to that date. For example, policies of this kind are taken out by persons who travel abroad, to cover shortperiod bank loans so that the sum assured will be available to repay the loan if the borrower die before the policy lapses, etc.

Joint Life Policy: This type of assurance involves the insurance of two lives simultaneously in the same policy. The sum assured (policy money) is payable by the insurer upon the death of any one of the

assured to the surviving person. If both the policy holders die at the same time, their legal heirs or nominees will be paid the assured sum.

Group Insurance: Under group insurance, a group of persons under the same employer are covered under a single policy. Premium is paid by the employer alone or by the employer and employee jointly. A group insurance policy may cover all the employees or a particular category/section of the employee of the same organisation. However, the employees are covered under this policy as long as they serve with that employer. In group insurance, the insurance contract is between the employer and the insurance company (insurer).

2)Marine Insurance: Marine insurance is an arrangement by which the insurer undertakes to compensates the owner of a ship or cargo for complete or partial loss at sea. Marine insurance covers ship, cargo and freight. Perils of the sea also includes any land risk incidental to sea voyage. Under marine insurance, insurable interest must exist only at the time of loss. It is not necessary for the insured to have the insurable interest at the time of taking the marine insurance policy. Marine insurance is a contract of indemnity.

Types of Marine Policies: The different kinds of marine policies are as follows:

Voyage Policies: This type of policy covers a ship or cargo during a specified voyage only. Thus the limits of the risk are from the port of departure to the port of destination. The risk which is covered starts from the departure of ship fiom the port and it ends when that ship reaches the port of destination.In the case of a voyage policy, issurer is not liable if the destination of the ship is changed or the ship deviates from the agreed route. However, deviation from the agreed route is allowed when it is necessary for the safety of ship/cargo or saving the human life or any other circumstance stated in the contract.

Time Policy: This type of policy covers the risk during a stated period of time irrespective of number of voyages made. This policy would cover all the risks from the perils of sea for a stated period of time.A time policy covers a period not more than 12 months. Most time policies include a contintiation clause providing against expiration of the policy if the ship is still on the voyage. A monthly prorata premium is payable for the continuation.

Mixed Policy: This combines the elements of a time policy and voyage policy. Mixed policy covers the risk during a particular voyage for a specified period.

Valued and Unvalued Policies: Under valued policy, the value of the subject matter insured (ship/cargo) is specified on the face of the policy. In the event of full loss the insurer compensates the amount specified in the policy. If the loss is partial a proportionate amount is paid by the insurer. On the other hand, in the case of an unvalued policy, the value of the subject matter is not stated in the policy. In case of loss or damage, the compensation is ascertained by assessment of loss, subject to the limit of the sum insured.

Floating Policies: This policy is suitable to a merchants who makes regular shipments. To avoid the botheration of taking a separate policy for every shipment, of exporter can take a floating Policy. A floating policy is taken for a round amount, and leaves the details to be declared at a later time, Whenever some cargo is shipped, the shiper (insured) makes a declaration stating the sum for which it is

to be insured. Then the total value of the floating policy is reduced by that amount. With each shipment, the value of the policy goes on decreasing.

3)Fire Insurance:Fire policies cover the losses directly caused through fire. However, it is necessary that fire must happen by ignition. If the fire is caused through the malicious act of the insured himself, he would not be able to recover the loss from the insurer. The fire insurance contract is an indemnity contract. In addition to fire, the standard fire policy covers such perils as lightning, explosion of domestic boilers, gas used for lighting and heating, and damage by water used to extinguish a fire on neighboring property. For a small additional premium the policy may be extended to cover such other items as storm and flood, earthquakes and impact from road vehicles or aircraft, but not glass and china, jewellery,manuscripts and other items of value, except where specially mentioned.Fire policy is for a fixed period. During that period if there are successive fire accidents, the insurer is liable to make good of all those successive losses.

Types of Fire Policies:

Specific Policy where the liability of the insurer is limited to a specified amount, which is normally less than the actual value of the property insured.

Valued Policy where the insurer agrees to pay a fixed amount in the event of loss, irrespective of the actual loss suffered. Under this policy, the insured recovers a fixed amount, irrespective of the amount of actual damage.

Floating Policy where the amount of the policy may vary from time to time. This type of policy is useful in the case of goods in store where quantity and value change from time to time.

Replacement Policy where the insurer has the option to replace the property/goods damaged by fire, instead of paying the loss by cash.

Loss of Profit Policy where insured is protected against the loss of profit due to dislocation of business due to fire. Under this policy, insurer compensates to the extent of the loss in profits.

Comprehensive Policy which provides cover against not only fire but also several other risks such as lightning, riot, earthquake, flood, storm, burglary, war, etc.

4)Motor Insurance: Owners of motor vehicles (two or four wheelers) can take insurance policies to cover different types of risks viz., (a) loss or damage to the vehicle, (b) injuries to or death of any passenger, and (c) damages payable to the third parties for accidents. Every motor-vehicle driver must be insured for against liability for death of or injury to third parties and for the cost of their medical surgica1 treatment.

5)Miscellaneous Insurance: There are several other types covering various other aspects of risks. Some of them are discussed below:

Engineering Insurance :This is a highly technical branch of insurance. It is a branch of insurance that has expanded rapidly under recent legislation and especially under the Factories Acts, which prescribe compulsory inspection at regular intervals of certain types of industrial equipment, such as boilers, electrical plant, cranes and other lifting gear.

Aviation Insurance: Under aviation insurance, cover is available for loss of or damage to aircraft,personal accidents to passengers, third party risks in respect of both person and property and for cargo sent by air.

(d) Letter of Credit

Ans: : Depending upon the terms of payment, the importer may have to arrange a letter of credit to be issued by his bank in favour of the exporter. All the terms and conditions agreed upon between the importer and exporter are generally spelt out in the letter of credit. The importer's bank issues the letter of credit authorising the correspondent bank in the exporter's country to buy the bill drawn by the exporter on the importer, or to accept the bill drawn on the bank itself. The importer's bank may require adequate amount to be deposited by the importer so as to cover the amount for which the letter of credit is issued. But such a deposit may not be insisted upon if the importer is an established person or a firm well known to the bank or it maintains a satisfactory deposit account with the bank.

A safer and quicker method of obtaining payment is that of documentary credit whereby the importer arranges for a bank to open a letter of credit in favour of the exporter. In a letter of credit, the importer's bank branch gives a written undertaking to the exporter that if the exporter presents certain documents relating to the shipment of the goods within a fixed period, the bank will honour the bill of exchange drawn under the credit upto the amount specified in the letter of credit. In both the cases, the necessary documents along with the bill of exchange drawn on the importer are sent to the importer through the exporter's bank. The negotiating bank scrutinizes the documents and thereafter sends the bill of exchange, bill of lading, insurance policy and other documents to the importer's bank for discharge of payment. If the bill is payable at sight, the exporter receives his money immediately. If it is payable certain number of days after sight or date, the bank accepts it and the exporter discounts it.