Section 1: Forms of Business Organizations

- There are three main forms of business organizations in the economy today— the sole proprietorship, the partnership, and the corporation.
- Each offers its owners significant advantages and disadvantages.

The most common form of business organization in the United States is the sole proprietorship or proprietorship—a business owned and run by one person.
- Although relatively the most numerous and profitable of all business organizations, proprietorships are the smallest in size.
- Proprietorships earn almost one-fifth of the net income earned by all businesses, even though they make only a fraction of total sales.

**Sole Proprietorships**
- The sole proprietorship is the easiest form of business to start because it involves almost no requirements except for occasional business licenses and fees.
- The advantages of a sole proprietorship include:
  - ease of starting up
  - relative ease of management
  - owner enjoys the profits of successful management
  - no separate business income taxes
  - psychological satisfaction
  - ease of getting out of business

- The disadvantages of a sole proprietorship include:
  - owner has unlimited liability—full and personal responsibility for all losses and debts of the business
  - difficulty in raising financial capital
  - size and efficiency—the business may have to carry a large inventory, or stock of finished goods and parts in reserve
limited managerial experience
– difficulty of attracting qualified employees
– limited life—firm ceases to exist when owner dies, quits, or sells the business

**Partnerships**

- A **partnership** is a business jointly owned by two or more persons.
- Partnerships are the least numerous form of business organization, accounting for the smallest proportion of sales and net income.

**Types of Partnerships**

- The most common form of partnership is a **general partnership**, one in which all partners are responsible for the management and financial obligations of the business.
- In a **limited partnership**, at least one partner is not active in the daily running of the business, although he or she may have contributed funds to finance the operation.
- Because more than one owner is involved, formal legal papers called **articles of partnership** are usually drawn up to specify arrangements between partners.

- The advantages of a partnership include:
  - ease of establishment
  - ease of management
  - lack of special taxes
  - attract financial capital easily
  - slightly larger size, increased efficiency
  - easier to attract top talent

- The disadvantages of a partnership include:
  - each partner is fully responsible for the acts of all other partners
  - limited partners have limited liability
  - limited life
  - potential for conflict between partners
  - offer increased access to financial capital, but do not always work out
  - A business may have to file for **bankruptcy**, a court-granted permission to an individual or business to cease or delay debt payments.

**Corporations**

- Corporations account for approximately one-fifth of the firms in the United States and about 90 percent of all sales.
- A **corporation** is a form of business organization recognized by law as a separate legal entity having all the rights of an individual.

**Forming a Corporation**

- Unlike a sole proprietorship or partnership, a corporation is a very formal and legal arrangement.
• People who would like to incorporate, or form a corporation, must file for permission from the national government or the state where the business will have its headquarters.
• If approved, a charter—a government document that gives permission to create a corporation—is granted.

• The charter also specifies the number of shares of stock, or ownership certificates in the firm.
• These shares are sold to investors, called stockholders or shareholders.
• The money is then used to set up the corporation.

If the corporation is profitable, it may eventually issue a dividend—a check representing a portion of the corporate earnings—to each stockholder.

Corporate Structure
• When an investor purchases stock, he or she becomes an owner with certain ownership rights.
The advantages of a corporation include:
  – ease of raising financial capital
  – gain capital by selling additional stock
  – borrow money by issuing bonds
• A bond is a written promise to repay the amount borrowed at a later date.
• The amount borrowed is known as the principal.
• While the money is borrowed, the corporation pays interest, the price paid for
  the use of another’s money.

The advantages of a corporation also include:
  – professional managers run the firm
  – limited liability for owners
  – unlimited life
  – ease of transferring ownership

The disadvantages of a corporation include:
  – difficulty and expense of getting a charter
  – owners have little say in how the business
    is run
  – double taxation of corporate profits, stockholders’ dividends are taxed
    twice—once as corporate profit and again as personal income
  – more government regulation

**Business Development**

State governments are very active in trying to attract new industry.
Governors often travel throughout the country or even to foreign countries to
draw new business to their states.
A state may offer an incentive such as a tax credit, or a reduction in taxes, in
return for the creation of new jobs or new business investment.

**Section 2:**

**Business Growth and Expansion**

A business can grow in one of two ways.
It can grow by reinvesting some of its
profits.
A business can also expand by engaging in a **merger**—a combination of two or
more businesses to form a single firm.

Most businesses use some of the revenue they receive from sales to invest in
factories, machinery, and new technologies.
We can use the **income statement**—a report showing a business’s sales,
expenses, and profits for a certain period—to illustrate the process.
The business first records its total sales for the period.
Next, it finds its **net income** by subtracting
all of its expenses, including taxes, from its revenues.
These expenses include the cost of goods and **depreciation**, a non-cash
charge the firm takes for the general wear and tear on its capital goods.
Reinvesting Cash Flows
- Depreciation is called a non-cash charge because, unlike other expenses, the money is never paid to anyone else.
- Cash flow, the sum of net income and non-cash charges such as depreciation, is the bottom line, or real measure of profits for the business.
- The cash flow represents the total amount of new funds the business generates from operations.
- Business owners decide how the cash flow will be allocated.
- When cash flows are reinvested in the business, the firm can produce additional products.
- As long as the firm remains profitable, and the reinvested cash flow is larger than the wear and tear on the equipment, the firm will grow.

Growth Through Mergers
- When firms merge, one gives up its separate legal identity.
- The name of the new company may reflect the identities of the merged companies.
  - A firm may seek a merger to grow faster, to become more efficient, to acquire or deliver a better product, to eliminate a rival, or to change its image.
  - Some companies merge in order to grow faster.
  - Efficiency is another reason for mergers.
  - Some mergers are driven by the need to acquire new product lines.
  - Sometimes firms merge to catch up with, or even eliminate, their rivals.
  - A company may use a merger to lose its corporate identity.
Types of Mergers

- Economists generally recognize two types of mergers:
  - The first is a horizontal merger, which takes place when two or more firms that produce the same kind of product join forces.
  - When firms involved in different steps of manufacturing or marketing join together, it is a vertical merger.

- A corporation may become so large through mergers and acquisitions that it becomes a conglomerate.

- A conglomerate is a firm that has at least four businesses, each making unrelated products, none of which is responsible for a majority of its sales.

- Other large corporations have become international in scope.

- A multinational is a corporation that has manufacturing or service operations in a number of different countries.

- They are important because they have the ability to move resources, goods, services, and financial capital across national borders.

Section 3: Other Organizations

- Most businesses use scarce resources to produce goods and services in hopes of earning a profit for their owners.

- Other organizations operate on a "not-for-profit" basis.

- A nonprofit organization operates in a businesslike way to promote the collective interests of its members rather than to seek financial gain for its owners.

- Examples of nonprofit institutions include organizations such as schools, churches, hospitals, welfare groups, and adoption agencies.

- Most of these organizations are legally incorporated to take advantage of unlimited life and limited liability.

- They are similar to profit-seeking businesses, but do not issue stock, pay dividends, or pay income taxes.

- They use scarce factors of production to serve many needs.
Cooperatives
Types of CO-OP’S
● Consumer cooperative:
  – The consumer cooperative is a voluntary association that buys bulk amounts of goods such as food and clothing on behalf of its members.
● Service cooperative:
  – A service cooperative provides services such as insurance, credit, and baby-sitting to its members, rather than goods. (Ex. Credit Union)
● Producer cooperative:
  – A producer cooperative helps members promote or sell their products.
Labor Unions
Professional Associations
● Many workers belong to professional societies, trade associations, or academies.
● One such organization is a professional association—a group of people in a specialized occupation that works to improve the working conditions, skill levels, and public perceptions of the profession.
● These associations also seek to influence government policy on issues that are important to them.
Business Associations
● Businesses also organize to promote their collective interests.
● Most cities and towns have a chamber of commerce that promotes the welfare of its members and of the community.
● Many business organizations represent specific kinds of businesses and are called industry or trade associations.
● Some business associations help protect the consumer.
● The Better Business Bureau, a nonprofit organization sponsored by local businesses to provide general information on companies, is one of these.
Government
● Direct Role of Government:
  – Many government agencies produce and distribute goods and services to consumers, giving government a direct role in the economy.
  – The role is “direct” because the government supplies a good or service that competes with private businesses.
  – Many federal agencies are organized as government-owned corporations.
Government
● Indirect Role of Government:
  – The government plays an indirect role when it acts as an umpire to make sure the market economy operates smoothly and efficiently.
  – One such case is the regulation of public utilities, investor- or municipal-owned companies that offer important products to the public, such as water or electric service.
  – The government also plays an indirect role when it grants money to people in the form of Social Security, veterans’ benefits, financial aid, and unemployment compensation.