

MODEL ANSWERS

AS-2608

B.Com. (Hons.) (First Semester)

Examination, 2013.

BUSINESS ORGANISATION

Note: Attempt five questions in all. Question No. One is compulsory carrying 20 marks. Remaining four questions carry 10 marks each.

1. Short answer type question. All compulsory. 2x10

(i) What is Commerce?

Ans. Commerce is the whole system of an economy that constitutes an environment for business. The system includes legal, economic, political, social, cultural and technological systems that are in operation in any country. Thus, commerce is a system or an environment that affects the business prospects of an economy or a nation-state. It can also be defined as a component of business which includes all activities, functions and institutions involved in transferring goods from producers to consumers.

(ii) What is reward for taking risk in business?

Ans. Profit is reward for taking risk in business.

(iii) What are two different components of Commerce?

Ans. Components of commerce includes:

(a) Trade : It is also called goods exchange of goods and services or transfer the ownership of goods from one person or entity to another by getting something in exchange from the buyer.

(b) Aids to Trade : Any economic activity which facilitates trade directly or indirectly such as transport, warehousing, insurance, banking, advertisement and communication etc are known as aids to trade.

(iv) What are Consumer goods?

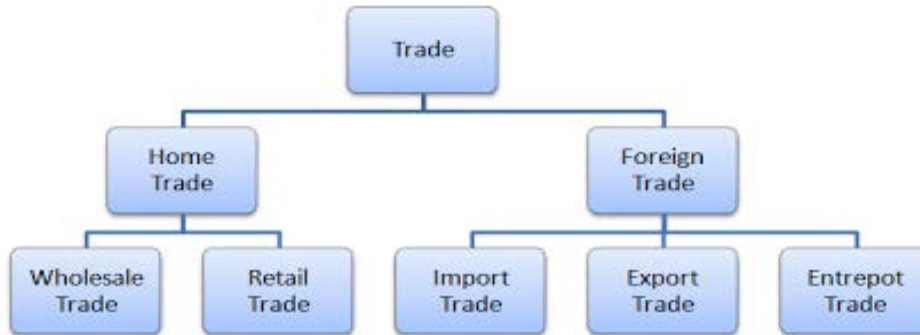
Ans. Consumer goods are tangible commodity produced and subsequently purchased to satisfy the current wants and perceived needs of the buyer. Consumer goods have a significant life span often three years or more.

(v) For which type of business, sole proprietorship form is more suitable?

Ans. Sole proprietorship form of business is suitable for small scale business like Grocery store, Stationary Shop, etc.

(vi) How would you classify trade on the basis of geographical area covered?

Ans. Trade on the basis of Geographical area covered trade are as follows:



Trade can be divided into following two types:

1. **Internal or Home or Domestic trade.**
2. **External or Foreign or International trade**

1. **Internal Trade:** Internal trade is also known as Home trade. It is conducted within the political and geographical boundaries of a country. It can be at local level, regional level or national level. Hence trade carried on among traders of Delhi, Mumbai, etc. is called home trade.

Internal trade can be further sub-divided into two groups:

(i)Wholesale Trade : It involves buying in large quantities from producers or manufacturers and selling in lots to retailers for resale to consumers. The wholesaler is a link between manufacturer and retailer. A wholesaler occupies prominent position since manufacturers as well as retailers both are dependent upon him. Wholesaler act as a intermediary between producers and retailers.

(ii)Retail Trade : It involves buying in smaller lots from the wholesalers and selling in very small quantities to the consumers for personal use. The retailer is the last link in the chain of distribution. He establishes a link between wholesalers and consumers. There are different types of retailers small as well as large. Small scale retailers includes hawkers, peddlers, general shops, etc.

2. External Trade

External trade also called as Foreign trade. It refers to buying and selling between two or more countries. For instance, If Mr. X who is a trader from Mumbai, sells his goods to Mr. Y another trader from New York then this is an example of foreign trade.

External trade can be further sub-divided into three groups:

(a) Export Trade : When a trader from home country sells his goods to a trader located in another country, it is called export trade. For e.g. a trader from India sells his goods to a trader located in China.

(b) Import Trade : When a trader in home country obtains or purchase goods from a trader located in another country, it is called import trade. For e.g. a trader from India purchase goods from a trader located in China.

(c) Entrepot Trade : When goods are imported from one country and then re-exported after doing some processing, it is called entrepot trade. In brief, it can be also called as re-export of processed imported goods.

(vii) What are the agglomerative factors of industrial location?

Ans. Agglomerative factors are those factors which attracts any particular business in a particular location such as availability of raw materials, better infrastructure, electricity, Banking, telecommunication, state policy, tax rebate etc.

(viii) What is a Pool?

Ans. A pool can be defined as a union of different companies in the same or similar arena of business. The main aim behind such 'coming together' is to limit competition among themselves in such a way that each company gets the maximum profits.

This is done by way of controlling of prices. The combining firms retain their distinct identity and autonomy in their internal management. Under pools all the factors that affect prices, whether directly or indirectly are considered.

(ix) Briefly explain any two evils (disadvantages) of combination.

Ans. Following are the disadvantages of business combination

1. Business combination brings monopoly in the market, which may be harmful for the society.

2. The identity of the old company finishes.
3. Goodwill of the old companies decrease, management of the company becomes difficult and it may result in over-capitalization.

(x) Describe in brief Diagonal Integration.

Ans. Diagonal Combination means integration of a main activity or process with ancillary activities and services. For instance, a newspaper company may integrate with transport company to ensure quick delivery of the newspaper to different parts of the country or an automobile plant may combine with a power generating unit. Thus, diversification of activities are diagonal. The purpose of diagonal integration is to ensure smooth and timely availability of ancillary services which are essential for the continuous working of the main units.

Long Answer Type Questions (Attempt any four)

10x4

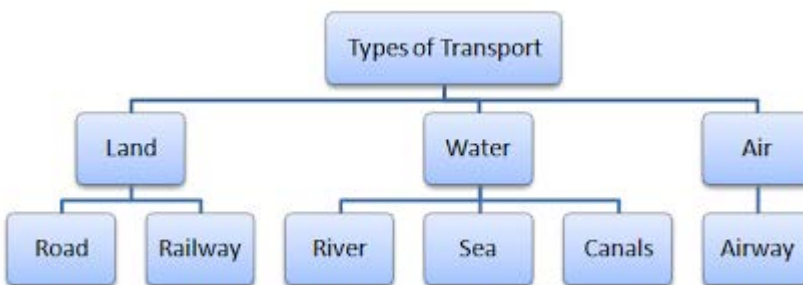
2. Explain various auxiliaries to trade in details?

Ans. The various **aids to trade** in commerce are explained in following points:

1. Transport:

In the modern times there is a vast distance between centers of production and centers of consumption. This difficulty is removed by an important aid to trade known as transport. Transport creates place utility.

There are several kinds of transport such as air, water and land transport. The geographical distance between producers and consumers is removed with the help of transport.



2. Communication:

Communication means transmitting or exchange of information from one person to another. It can be oral or in writing. It is necessary to communicate information from

one to another to finalize and settle the terms of sales such as prices of goods, discount allowed, facility of credit, etc.

Modern means of communication like telephone, telex, telegraph, email, teleconference, etc., plays an important role in establishing contact between businessman, producers and consumers.

3. Warehousing:

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. Agricultural commodities like wheat and rice are seasonal in nature but are consumed throughout the year, on the other hand goods such as umbrellas and woolen clothes are produced throughout the year but are demanded only during particular seasons. Therefore goods need to be stored in warehouses till they are demanded. So it creates time utility by supplying the goods at right time to consumer.

4. Insurance:

Insurance reduces the problem of risks. Business is subject to risks and uncertainties. These are inevitable in the field of business. Risks may be due to fire, theft, accident or any other natural calamity. Insurance companies who act as risk bearer cover risks. Insurance tries to reduce risks by spreading them out over a greater number of people. The rate of premium depends upon the type of risks and the period for which the risk is covered.

5. Banking:

Banking solves the problem of finance. Businessmen receives money and also pays money in large amounts. It is risky to carry large amount of cash from one place to another. Here comes Banking as a solution. Banking and financial institutions solves the problem of payment and facilitate exchange between buyer and seller. The businessmen may also require short-term and long-term funds. Banks provide such finance to businessmen. Banks also advances loans in the form of overdraft, cash credit and discounting of bills of exchange.

6. Advertising:

Advertising fills the knowledge gap and it solves the difficulty of information. Exchange of goods and services possible only if producers can bring the products to the consumers. Advertising and publicity are important medias of mass communication. Advertising helps the consumers to know about the various brands manufactured by several manufacturers. The medias used to advertise products are Radio, Newspapers, Magazines, TV, Internet, etc.

7. Salesmanship:

It facilitates personal selling. Many a times sales force is required to book orders directly from dealers or customers. Salesmanship is very much required in the sales of services and industrial goods. Again the sales force plays an important role in direct marketing, especially in the case of selling insurance policies

8. Mercantile Agents:

It removes personal difficulties. Mercantile agents are middlemen who form a link between the buyers and the sellers. They do not carry on business in their own name. In the process of distribution, producers and consumers are unable to have direct contact, as consumers are spread over a vast area. Mercantile agents remove this difficulty of personal contact.

There are several types of mercantile agents such as brokers, commission agents, auctioneers, underwriters, insurers, etc.

9. Trade Promotion Organizations in a Country:

They attend to difficulties of promotion and development of trade at national level. These are the organizations established by the business community to protect and promote their interest. They play promotional and developmental role for members. They do market research work, act as clearing house of information, put their grievances before the government, make representations, and help business community in many ways.

The examples include Chambers of Commerce, Export Promotion Councils, Indian Institute of Packaging, etc.

10. Global Organizations for International Trade: They attend to promotion and development of trade at international level. The main objective of global organizations is to promote International trade. It helps exporters and importer by collecting information about international marketing trends.

The examples of such global organizations are World Bank, IMF, WTO, etc.

3. Define Sole Proprietorship? Explain its merits and limitations.

Ans. A Sole Proprietorship is a simple type of business structure that is owned and operated by the same person. It does not involve many of the complex filing requirements associated with other types of business structures such as corporations. Sole proprietorships allow persons to report business income and expenses on their individual tax returns.

Sole proprietorships are attractive to small investors because they are relatively easy to start up. Also, the owner is entitled to all the profit that the sole proprietorship collects. On the other hand, sole proprietorships can be risky because there is no separation between the owner and the business.

In other words, the owner remains personally liable for any losses or debts that the sole proprietorship incurs. They can also be held legally responsible for violations committed by the business or its employees

Advantages of a Sole Proprietorship:

There are many reasons why a person would choose to start their business up using a sole proprietorship structure. Some of the main advantages of sole proprietorships include:

- **Ease of formation:** Starting a sole proprietorship is much less complicated than starting a formal corporation, and also much cheaper. Some states allow sole proprietorships to be formed without the double taxation standards applicable to most corporations. The proprietorship can be named after the owner, or a fictitious name can be used to enhance the business' marketing
- **Tax benefits:** The owner of a sole proprietorship is not required to file a separate business tax report. Instead, they will list business information and figures within their individual tax return. This can save additional costs on accounting and tax filing. The business will be taxed at the rates applied to personal income, not corporate tax rates
- **Employment:** Sole proprietorships can hire employees. This can lead to many of the benefits associated with job creation, such as tax breaks. Also, spouses of the business owner can be employed without having to be formally declared as an employee. Married couples can also start a sole proprietorship, though liability can only assumed by one individual
- **Decision making:** Control over all business decisions remains in the hands of the owner. The owner can also fully transfer the sole proprietorship at any time as they deem necessary.

4. What are the preliminary considerations which you should keep in mind while opting for a particular form of business organization ?

Ans. A business enterprise can be owned and organized in several forms. Each form of organization has its own merits and demerits. The ultimate choice of the form of business depends upon the balancing of the advantages and disadvantages of the various forms of business. The right choice of the form of the business is very crucial because it determines the power, control, risk and responsibility of the entrepreneur as well as the division of profits and losses. Being a long term commitment, the choice of the form of business should be made after considerable thought and deliberation.

The choice of the form of business is governed by several interrelated and interdependent factors :-

1.The Nature of Business :It is the most important factor. Businesses providing direct services like tailors, restaurants and professional services like doctors, lawyers are generally organized as proprietary concerns. While, businesses requiring pooling of skills and funds like accounting firms are better organized as partnerships. Manufacturing organizations of large size are more commonly set up as private and public companies.

2.Scale of Operations : Volume of business (large, medium, small) and size of the market area (local, national, international) served are the key factors. Large scale enterprises catering to national and international markets can be organized more successfully as private or public companies. Small and medium scale firms are generally set up as partnerships and proprietorship. Similarly, where the area of operations is wide spread (national or international), company ownership is appropriate. But if the area of operations is confined to a particular locality, partnership or proprietorship will be a more suitable choice.

3.The Degree of Control: A person who desires direct control of business, prefers proprietorship, because a company involves separation of ownership and management.

4.Amount of Capital : The amount of capital required for the establishment and operation of a business. A partnership may be converted into a company when it grows beyond the capacity and resources of a few persons.

5.The Volume of Risks : The volume of risks and liabilities as well as the willingness of the owners to bear it is also an important consideration.

6.Comparative Tax Liability. All of the forms of business organizations can be separated into two groups: **corporations where tax is assessed at the corporate level and "pass-through entities" where tax is assessed at the shareholder level.** The phrase "pass-through entity" means that profits are not taxed to business entity. Instead, the profits (or losses) are imputed as income (or "passed-through") to the owners. Each owner reports his or her share of profits or losses on his or her individual tax return.

Here's the breakdown of the various types of organizations.

Organizations that are taxed at the corporate level:

- **Corporations,**
- **Limited Liability Companies taxed as corporations, and**

- **Non-profit organizations**

Organizations that are taxed at the owner level ("Pass-through entities"):

- **Sole proprietors,**
- **S-Corporations,**
- **Partnerships, and**
- **LLC/LLP/PLLC/PLLP taxed as partnerships**

5.What do you mean by business combinations? Explain the merits and demerits of business combinations.

Ans.

The main objective of business combination is to eliminate cut-throat competition and secure the advantages of large scale production. Following are the advantages of business combination.

1. Competition between and among the companies will be eliminated.
2. Amount of capital can be increased by combining business.
3. Establishment and management cost can be reduced.
4. Benefits of large scale production can be secured.
5. Operating cost can be reduced by avoiding duplication.
6. Research and development facilities are increased.
7. Monopoly in the market can be achieved.
8. Bulk purchase of materials at reduced price is possible.
9. Stability of the price of goods is maintained.

Following are the disadvantages of business combination

1. Business combination brings monopoly in the market, which may be harmful for the society.
2. The identity of the old company finishes.
3. Goodwill of the old companies decrease.
4. Management of the company becomes difficult.
5. Business combination may result in over-capitalization.

6. Discuss various factors which affects the location of an industrial unit.

Ans. Factors Influencing Industrial Location:

Generally, location of industries is influenced by economic considerations though certain non-economic considerations also might influence the location of some industries. Maximisation of profit which also implies cost minimization is the most important goal in their choice of particular places for the location of industries. There are several factors which pull the industry to a particular place. Some of the major factors influencing location are discussed below:

1. Availability of raw materials: In determining the location of an industry, nearness to sources of raw material is of vital importance. Nearness to the sources of raw materials would reduce the cost of production of the industry. For most of the major industries, the cost of raw materials form the bulk of the total cost. Therefore, most of the agro-based and forest-based industries are located in the vicinity of the sources of raw material supply.

2. Availability of Labour: Adequate supply of cheap and skilled labour is necessary for and industry. The attraction of an industry towards labour centres depends on the ratio of labour cost to the total cost of production which Weber calls 'Labour cost of Index'. The availability of skilled workers in the interior parts of Bombay region was one of the factors responsible for the initial concentration of cotton textile industry in the region.

3. Proximity to Markets: Access to markets is an important factor which the entrepreneur must take into consideration. Industries producing perishable or bulky commodities which cannot be transported over long distance are generally located in close proximity to markets. Industries located near the markets could be able to reduce the costs of transport in distributing the finished product as in the case of bread and bakery, ice, tins, cans manufacturing, etc. Accessibility of markets is more important in the case of industries manufacturing consumer goods rather than producer goods.

4. Transport Facilities: Transport facilities, generally, influence the location of industry. The transportation with its three modes, i.e., water, road, and rail collectively plays an important role. So the junction points of water-ways, roadways and railways become humming centres of industrial activity. Further, the modes and rates of transport and transport policy of Government considerably affect the location of industrial units. The heavy concentration of cotton textile industry in Bombay has been due to the cheap and excellent transportation network both in regard to raw materials and markets.

5. Power: Another factor influencing the location of an industry is the availability of cheap power. Water, wind, coal, gas, oil and electricity are the chief sources of power. Both water and wind power were widely sought at sources of power supply before the invention of steam engine. During the nineteenth century, nearness to coal-fields became the principal locating influence on the setting up of new industries, particularly, for heavy industries. With the introduction of other sources of power like electricity, gas, oil, etc. the power factor became more flexible leading to dispersal and decentralization of industries.

6. Site and Services: Existence of public utility services, cheapness of the value of the site, amenities attached to a particular site like level of ground, the nature of vegetation and location of allied activities influence the location of an industry to a certain extent. The government has classified some areas as backward areas where the entrepreneurs would be granted various incentives like subsidies, or provision of finance at concessional rate, or supply of power at cheaper rates and provision of education and training facilities. Some entrepreneurs induced by such incentives may come forward to locate their units in such areas.

7. Finance: Finance is required for the setting up of an industry, for its running, and also at the time of its expansion. The availability of capital at cheap rates of interests and in adequate amount is a dominating factor influencing industrial location. For instance, a review of locational history of Indian cotton textile industry indicates that concentration of the industry in and around Bombay in the early days was mainly due to the presence of rich and enterprising Parsi and Bhatia merchants, who supplied vast financial resources.

8. Natural and Climatic Considerations: Natural and climatic considerations include the level of ground, topography of a region, water facilities, drainage facilities, disposal of waste products, etc. These factors sometimes influence the location of industries. For instance, in the case of cotton textile industry, humid climate provides an added advantage since the frequency of yarn breakage is low. The humid climate of Bombay in India and Manchester in Britain offered great scope for the development of cotton textile industry in those centres.

9. Personal Factors: In deciding location of industrial units, sometimes an entrepreneur may have personal preferences and prejudices against certain localities. For instance, Mr. Ford started to manufacture motor cars in Detroit simply because it was his home-town. In such cases, personal factor dominates other considerations. However, this kind of domination is rare.

10. Strategic Considerations: In modern times, strategic considerations are playing a vital role in determining industrial location. During war-time a safe location is assuming special significance. This is because in times of war the main targets of air attacks would be armament and ammunition factories and industries supplying other commodities which are required for war. The Russian experience during the Second World War provides an interesting example.

11. External Economies: External economies also exert considerable influence on the location of industries. External economies arise due to the growth of specialized subsidiary activities

when a particular industry is mainly localized at a particular centre with port and shipping facilities. External economies could also be enjoyed when a large number of industrial units in the same industry were located in close proximity to one another.

12. Miscellaneous Factors: Historical incidents also play a dominating role in determining the location of industries in certain cases. The development of cotton-textile industry in Lancashire provides an interesting example for this. Further, the size of and industrial unit would also have much influence in choosing location. This is because the size of industrial units depends upon the radius of the circle within which they can profitably distribute their goods and upon the density of population living within the circle.

7. “Business combination leads to monopoly” do you agree? Give reasons to support your answer.

Ans.

If we look at the basic inclination of the capitalist economy it is towards the development of mass production, growth of specialization, use of machinery and computers. There is also stiff competition among producers for the marketing of products resulting in lowering of the prices. The competition among the producers has given place to business combinations.

Business combination is basically the voluntary association of firms for the achievement of common goals. The combination among the firms may be temporary or permanent. The combination may be formed by a written agreement among the firms, or there may be oral understanding among them to unite for enjoying the advantages of monopoly. Causes of business combinations can be many.

Elimination of competition:

Nowadays, a large number of firms produce a particular type of commodity. The competition among the firms leads to goods being sold at out throat prices. The stiff competition among the producers has increased the capital risk and lowered the profits of the firms.

Some of the other causes associated with the business combination are as follows:

- *Economies of large scale productions**
- *Changes in economic policy**
- *Fluctuations in business activity**
- *Influence of tariffs**
- *Formation of joint stock companies**
- *Transport developments**
- *Patent laws**
- *Rationalization**
- *Respect for bigger units**

***Students are required to give relevant explanation accordingly.**

8. Critically examine Weber's deductive theory of industrial locations.

Ans. Alfred Weber, a German economist, enunciated a systematic theory of industrial location in 1909. Weber's theory of location is purely deductive in its approach. He analyzed the factors that determine the location of industry and classified these factors into two divisions. These are:

(i) Primary causes of regional distribution of industry (regional factors)

(ii) Secondary causes (agglomerative and deglomerative factors) that are responsible for redistribution of industry.

(i) Primary Causes (Regional Factors)

According to Weber, Transport costs and Labour costs are the two regional factors on which his pure theory is based. Assuming that there are no other factors that influence the distribution of industry, except transportation costs. Then it is clear that the location of industry will be pulled to those locations which have the lowest transportation costs. The key factors that determine transportation costs are

(i) the weight to be transported and

(ii) the distance to be covered.

Weber lists some more factors which influence the transportation costs such as – (a) the type of transportation system and the extent of its use, (b) the nature of the region and kinds of roads, (c) the nature of goods themselves, i.e., the qualities which, besides weight, determine the facility of transportation.

However, the location of the place of production must be determined in relation to the place of consumption and to the most advantageously located material deposits. Thus, 'locational figures' are created. These locational figures depends upon (a) the type of material deposits and (b) the nature of transformation into products.

Weber classifies and calls those raw materials, which are available practically everywhere as 'ubiquities' (like brick-clay, water, etc) and 'localised' (like iron-ore, minerals, wood, etc) which are available only in certain regions. It is clear that localized materials play a more important

role on the industry than the ubiquities. Further, regarding the nature of the transformation of materials into products, Weber categorized the raw materials as 'pure' and 'weight losing'. Pure materials impart their total weight to the products (eg. cotton, wool, etc) and the materials are said to be 'weight losing' if only a part enters into the product (eg. wood, coal, etc.). Hence, the location of industries using weight-losing materials is drawn towards their deposits and that of industries using pure-materials towards the consumption centres.

Weber further examines the cause of deviation of industrial location from the centres of least transport costs. The existence of differences in labour costs leads an industry to deviate from the optimal point of transport orientation. Geographical distribution of the population would give rise to differences in wages for labour. Naturally, the transport oriented location of an industry is drawn out and attracted towards the cheaper labour centres. Such migration of an industry from a point of minimum transport costs to a cheaper labour centre may be likely to occur only where the savings in the cost of labour are larger than the additional costs of transport which it ought to incur.

(ii) Secondary Causes (Agglomerative and Deglomerative Factors)

An agglomerative factor is an advantage or a cheapening of production or marketing which results from the fact that production is carried on at one place. A deglomerative factor is a cheapening of production which results from the decentralization of production i.e., production in more than one place. To some extent these agglomerative and deglomerative factors also contribute to local accumulation and distribution of industry. These factors will operate only within the general framework formed by the two regional factors, i.e., costs of transportation and costs of labour. The advantages which could be derived in this context are external economies.

The pulls which the agglomerative factors possess to attract an industry to a particular point are mainly dependent on two factors. Firstly, on 'the index of manufacture' (the proportion of manufacturing costs to the total weight of the product) and secondly, on the 'locational weight' (the total weight to be transported during all the stages of production). To deduce a general principle, Weber uses the concept of "co-efficient of manufacture" which is the ratio of manufacturing cost to locational weight. Agglomeration is encouraged with high co-efficient of manufacture and deglomeration with low co-efficient of manufacture and these tendencies are inherent in their nature.

Criticisms:

Weber's theory of location has been criticized on various grounds which may be summarized as follows:

1. Weber has been criticized for his unrealistic approach and deductive reasoning. According to Sargant Florence, vague generalizations cannot provide suitable solutions to the theory of location as non-economic considerations will also influence which are not mentioned in the

pure theory. He says that Weber's theory fails to explain locations resulting from historical and social forces.

2. A. Predohl criticizes Weber's theory as more a selective theory than a deductive theory. The very distinction between primary and secondary is itself artificial, illogical and arbitrary.

3. Weber assumes fixed labour centres and unlimited supplies of labour which are unrealistic. The rise of industry may create new labour centres and we cannot assume unlimited labour supplies at any centre.

4. In a competitive market structure, the assumption of fixed points of consumption is unrealistic. Country-wise scattering, usually, of consuming public is a reality and there may be a shift in the consuming centres with a shift in industrial population.

5. A. Robinson also considers Weber's division of raw materials into 'ubiquities' and 'localised' as artificial.

Weber's deductive theory of location, in spite of the shortcomings, is the only theory which has been enjoying the universal acceptance and application, as all the other alternative suggestions are neither complete nor comprehensive.

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