1.2 What is a business?

Businesses are key players in the economy. They provide people with employment, and create **goods** and **services** for consumers (like us), enabling us to satisfy our needs and wants.

A business is any organisation that produces and sells, for a profit, the goods and services that satisfy the needs and wants of consumers. Your local butcher is a business, as is the supermarket you shop in and the local video store.

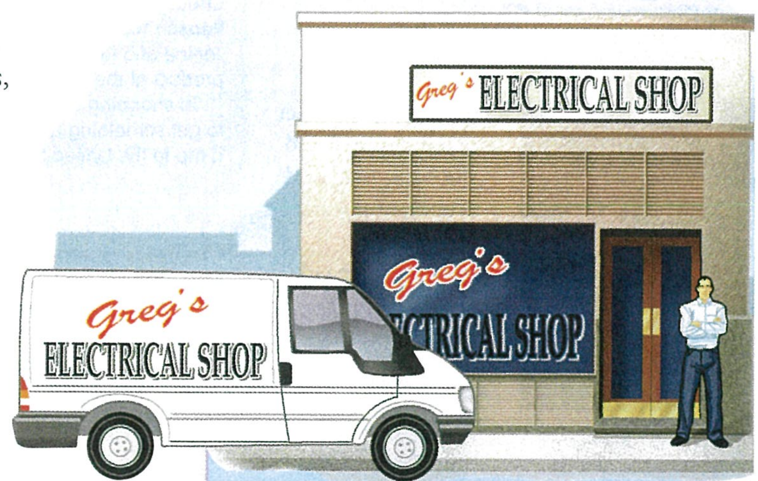
Some organisations operate in order to provide social, educational, religious or other services rather than to earn a profit. The Salvation Army and World Vision are examples. Such 'businesses' are called non-profit organisations.

There are many different types of business, all designed to suit the particular needs of the people who establish them. These include sole traders, partnerships, and public and private companies. Businesses have different structures and legal responsibilities and it is important to understand the differences, for example, between a **limited liability** company and a private enterprise operation.

What are the main types of businesses?

There are four main types of businesses: sole trader, partnership, public company and private company. These are described below.

Sole trader

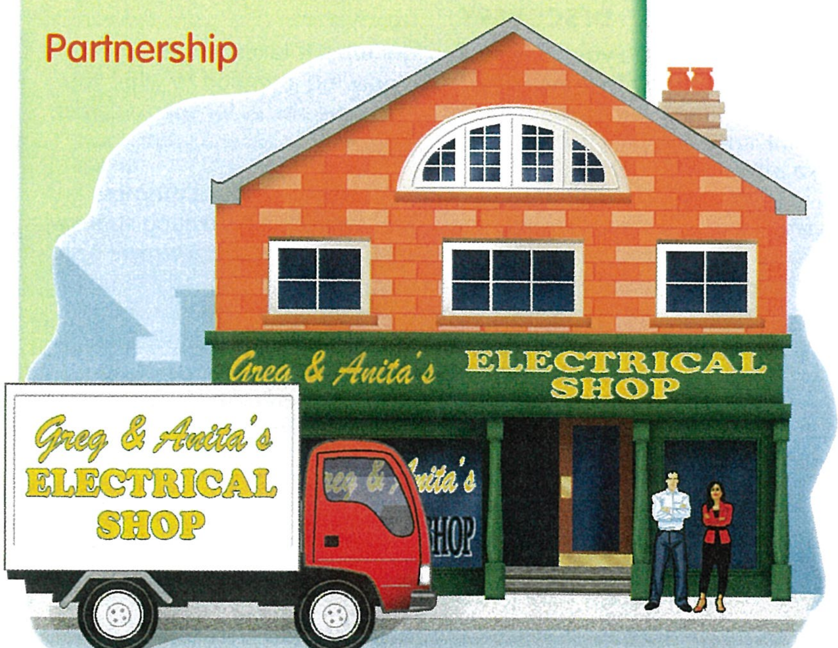


A *sole trader* is a business that is owned by one person, even though it may employ other people to operate and manage the business. It is the most common type of business in Australia. A sole trader business can operate in almost any field. Usually, however, they are stores, cafes, newsagents and hairdressers as well as trades such as plumbers and electricians.

The sole trader receives all the profit and suffers all the losses. He or she has unlimited liability. This means he or she can be forced to sell personal assets such as the house or car to pay off business debts. A sole trader usually has only one person's name in its business name, for example Maria's Cafe.

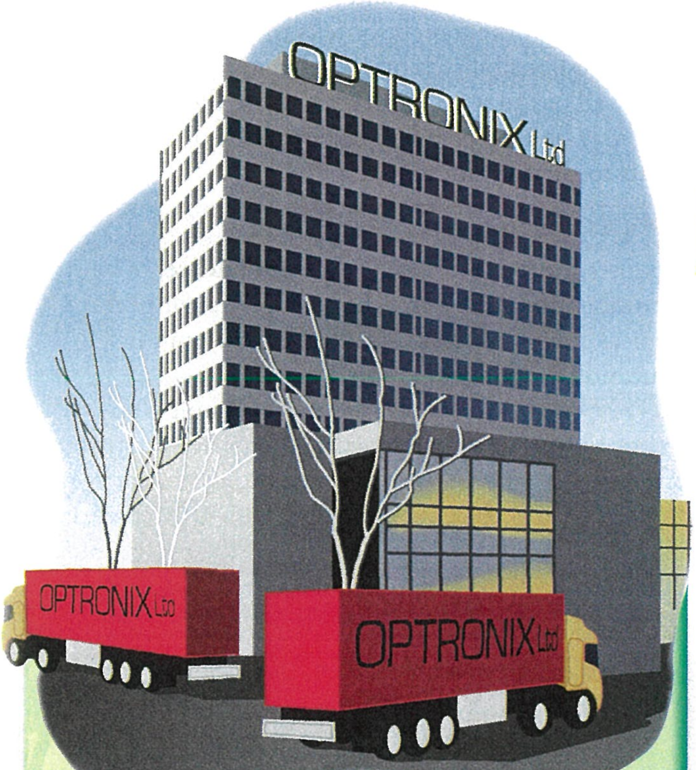
A *partnership* is a business usually owned and operated by two or more people, called partners. The partners share their profits and losses, usually equally. Together they decide how best to operate the business. It is common for people with similar skills, such as doctors, accountants, solicitors and dentists, to form a partnership. Partnerships tend to have the names of the partners in the business name. Partnerships have unlimited liability.

Partnership



In Australia, all companies undergo a process known as incorporation. This involves creating a business as a legal entity in its own right and treating it as a separate entity from its shareholders. In other words, the company (rather than individual shareholders) is liable for the debts created through its operation. There are two major forms of companies in Australia: public companies and private companies.

Public company



A *public company* can have an unlimited number of shareholders. The general public may buy and sell shares in these companies. This is done through the **stock exchange**. Most public companies are large and attract investment quickly. Examples include Westfield, Billabong and Woolworths. Shareholders in public companies have limited liability.

A public company must have the word 'Limited', abbreviated to 'Ltd', after its name.

Public companies can have an unlimited number of shareholders. There is no restriction on transfer of **shares** between people or the amount of money that can be raised through offering shares. A **prospectus** is issued when selling shares. The minimum requirement (under the law) is that it have three directors, two of whom must live in Australia. A public company is also required to publish an annual report that clearly states its financial position.

Proprietary (private) company

A *proprietary (private) company* usually has between two and 50 private owners called shareholders. These businesses tend to be small to medium in size. Often they are family-owned. Shares in private companies are offered only to those people the business wants as part-owners. Shareholders can sell their shares only to people who have been approved by the owners. This is why it is called a 'private' company.

A private company must have the words 'Proprietary Limited', abbreviated to 'Pty Ltd', after its name. They are not listed on the stock exchange. The main advantage of a private company is that shareholders have limited liability. This means that if the business cannot pay its debts, a shareholder loses only the money she or he has invested in the business.

So a shareholder cannot be forced to sell personal **assets** to pay the company's debts. However, there are some exceptions to this situation. In some instances, the directors of the company will be asked to give a personal guarantee when financial institutions are giving loans. In these cases, the person who offered the personal guarantee might lose their own assets to pay the debts of the business.

If company directors engage in misleading behaviour or recklessly borrow money, they can be held personally responsible. Criminal charges may follow, with lawsuits being brought under the code of civil law.

Other types of businesses

Franchises

In recent times, franchising has also become a very popular form of business structure. A franchisor is the individual or organisation that grants the franchise, and the franchisee is the person who purchases the franchise. Most franchisees then operate their business either as a sole trader or in partnership with another person.

The benefit to the franchisee is that he/she is granted an instantly recognisable business name (e.g. Subway, Hungry Jack's) and can immediately start to draw on the goodwill of that business. The franchisee also receives training in the technical aspects of operating the business from the franchisor, as well as assistance with business management principles. In return, the franchisee provides the start-up fees and labour, and agrees to uphold the terms and conditions of the franchise agreement. This means, for example, that a franchisee is obliged to market and sell the products and/or services specified under the franchise agreement and conform with any required production and distribution processes and requirements.

Just as there are many advantages for businesses operating as franchises, there are also disadvantages for both the franchisee and franchisor.

Operating a business as a franchise limits the **autonomy** of an individual franchisee in relation to marketing. For example, when you enter a McDonald's Restaurant, the décor looks the same, the staff act, sound and look the same, and the food tastes the same as in any other McDonald's anywhere in Australia. Operating a franchise limits the owner's ability to innovate and individualise their stores.

All advertising and promotional campaigns are run from a centralised office and must be run in all franchise stores in exactly the same way. An owner of a franchise may not agree with a particular TV commercial or a Scratch and Win promotion, but they must do what the franchisor tells them.

The responsibility is on the operator/franchisee to follow all of the strict guidelines set by the franchisor or they may be reprimanded, receive a fine or even lose the rights to their business.

Cooperatives

Another form of business is the **cooperative**, in which a number of people combine for a particular purpose. Typical cooperatives involve farmers, community education centres and **credit unions**.

The benefit of a cooperative is that people who work in one industry can join together to manage their own affairs, drawing on their combined expert knowledge of the specialist aspects of their work. They also reduce costs by streamlining their operations to ensure maximum efficiency in the delivery of goods and services.

FIGURE 1

Some franchise operations in Australia include Aussie Pooch Mobile, a dog-washing business, and Jim's Mowing, one of several divisions of Jim's Group, which provides home services.

There are many different types of cooperatives used for a wide range of purposes, including cooperatives for housing, building, consumers, workers and credit unions. Retailers' cooperatives buy in bulk on behalf of their members to obtain discounts from manufacturers and to pool marketing. This type of cooperative is common for locally owned grocery stores, hardware stores and pharmacies. However, their members are businesses rather than individuals. An example of a retailers' co-op is the Best Western international hotel chain whose members are hotel operators (see figure 2). The members own and operate their own businesses but work together and pool funds and resources through Best Western, which operates as a non-profit organisation. Pooled funds are used to advertise their businesses and the Best Western brand, and to generate greater buying power.

FIGURE 2

The Best Western hotel chain is an example of a retailers' cooperative.

asset an item or a resource of value
autonomy independence or freedom
cooperative a jointly owned commercial enterprise formed when a number of people in the same industry combine to produce goods and services
credit union a financial institution, often linked to an industry, that manages funds and acts as a lender; it is not a bank
goods merchandise, commodities for sale or trade; items that you can see or touch
limited liability shareholders cannot lose more than their investment in the event of the failure of the business
prospectus an official document issued by a company that explains the company structure and invites investment from the public
services work done by one individual or business and sold to another, such as an accountant or plumber (generally intangible goods of economic value); actions done for you by others
shares units of ownership in a company. An investor may purchase a great many, or only a few, of these units. As the value of a company's shares goes up or down, so too does the value of the shareholder's investment.
stock exchange a market where stocks, bonds and other securities are bought and sold

Activities

Student worksheet 1.2

REMEMBER

1 Define in your own words:
(a) proprietary company
(b) limited liability
(c) public company.
2 What are the main differences between a private and a public company?
3 Write the following words in a sentence to show you understand their meaning:
(a) incorporation
(b) goodwill
(c) franchisee
(d) franchisor
(e) cooperative.

THINK

4 Why do you think the law requires that at least two directors of Australian public companies live in Australia?
5 Outline the main advantages and disadvantages in establishing a business through a franchise agreement.
6 What are the benefits to farmers of joining a cooperative?
7 Most farms are registered as businesses. Why would this be so?
8 Under what circumstances will the directors of a company be personally liable for the company's debts in the event of a collapse?

COMMUNICATE

9 Copy the table below into your notebook and rearrange so that the correct term is next to the correct example. Use the information on pages 6–9 to help you.

Cooperative	A small bicycle shop which offers personal and professional advice
Public company	A suburban hairdresser
Franchise	A national retail chain that would require $600 million to establish
Sole trader	A medical clinic
Private company	A community book exchange
Partnership	A fast food outlet

ICT

10 Work in groups for this activity. Choose a business that interests you — it may be a local, national or international business. Use specialised search techniques to find out as much as you can about it on the internet and through other means. Share your findings with your group.
- What type of business is it, and how is it structured?
- What are some of the business's key products/services?
- What else about this business is of particular interest?