COMMERCE

HIGHER SECONDARY- SECOND YEAR

Untouchability is a Sin

Untouchability is a Crime

Untouchability is Inhuman

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PREFACE

This book on commerce meant for the XII Standard students has been written in accordance with the revised and enriched syllabus. Since the study of commerce has undergone a sea change in the recent past, it has become inevitable to bring out a standard book on commerce covering all the latest topics. Chapters on forms of business organisation like sole trader, partnership, cooperatives and joint stock companies have been discussed in detail to enable the teachers and the students to acquaint with the latest development in the subject. The role of Government in business has been elaborately dealt in this book to create an awareness in the minds of the readers to keep pace with the recent innovative developments.

It is highly appreciable that senior and experienced teachers in the field have been selected to provide the required inputs to the book, keeping in view of changing needs of the society.

The syllabus of plus-two commerce has been divided to depict every aspect of the syllabus in detail. The subject matter is presented in a lucid style which would enable the students to understand the subject easily. Further to create an awareness in the minds of students and investors, chapters on Stock Exchange and SEBI have been elucidated in this book which would safeguard their interests. The recent amendments in the law relating to cooperatives and joint stock company are duly incorporated to give an upto-date information about the changes.

Charts, diagrams and down-loaded pictures have been included in appropriate places for a better understanding of the subject.

We believe that some extra efforts are required from our teachers while teaching new chapters. We solicit the teachers to offer their esteemed opinion and criticism about this book.

While preparing for the examination students should not restrict themselves only to the questions given in the self- evaluation. They must also be prepared to answer the questions and problems from the entire text.

We hope that the book is rich in its content and quality which will enhance the knowledge of the students.

CHAIR PERSON

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CHAPTER - 1
ORGANISATION

"The business is coming to realise that, education is to business what fertiliser is to farming"

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 1.1. Meaning of business organisation
- ❖ 1.2. Principles of organisation
- ❖ 1.3. Types of organisation

1.1. MEANING OF BUSINESS ORGANISATION

Literally speaking, business means " State of being busy" throughout. In economic sense, the word business means work efforts and acts of people which are connected with the production of wealth. Functionally, " those human activities which involve production or purchase of goods with the object of selling them at a profit." are called business.

The term business organisation is very often used in different senses. Firstly it is used to represent a business enterprise such as Tata Iron & Steel. " Secondly business organisation is a subject of study consisting of topics concerned with organisation and management of industrial and commercial organisation. Thirdly, the term 'Organisation' is used to mean bringing together various elements of business with the object of establishing harmonious relationship and adjustment in their functioning.

OBJECTIVES

The objects of business organisation are

1. Profit motive
2. Service motive
3. To get the economies of large scale production

4. To achieve in time and efforts
5. Harmonious relations with employees

FUNCTIONS

The important functions of business are as follows

1. Production function
2. Marketing function
3. Finance function
4. Personnel function
5. Purchase function
6. Public relations function
7. Legal function

Sound organisation is essential for the success of a business. The reason is that it makes administration easy. It consists of determining the activities to be undertaken for achieving the objectives. The activities are arranged in groups. Each group of activities are entrusted to each department. The duties and functions of each individual in each department are defined. So organisation consists of department and grouping of activities, delegation of work and establishment of relationship between various persons.

The word organisation has originated from the word 'organism' which means any system with parts dependent upon each other. In a human body, it is the brain which controls, directs and co-ordinates the activities of different parts of the body. The human body is a combination of various limbs. If any one of the limbs stops functioning properly, then some defects will develop in the body. If the goals of an enterprise are to be achieved, the activities of the different departments must be welded together. Organisation does this co-ordination. It establishes inter-relations between departments.

DEFINITION:

According to Urwick and Hunt, "A business is an enterprise which makes, distributes or provides an article or service which other members of the community need and are able and willing to pay for it".

According to Lewis H.Haney, "Organisation is a harmonious adjustment of specialised parts for the accomplishment of some common purpose or purposes"..

Louis A. Allen has defined organisation as "the process of identifying and grouping the work to be performed, defining and delegating responsibility and

authority and establishing relationship for the purpose of enabling people to work most effectively together in accomplishing objectives".

Organisation means finding out the objectives, grouping the activities aimed at their achievement, assigning them for performance and coordinating them are the features of an organisation. The study of organisation is important for the following reasons.

a) Organisation pervade all the important phases of human life. A man is born in organisation (hospitals and clinics). He is educated in an organisation (Schools, Colleges and universities). He works in an organisation (office, factories and business).

b) Knowledge of organisation helps the manager to work effectively.

c) Organisation satisfies and sometimes frustrates, if it is not well organised.

1.2. PRINCIPLES OF ORGANISATION

The following principles are helpful in developing a sound and efficient organisation to achieve the objectives of the business successfully.

1. Unity of Objectives

The term objective means a goal to be achieved.The organisation structure depends upon the objectives of the enterprise. Therefore the objectives of an enterprise must be clearly fixed. Every part of the organisation should be designed to facilitate the accomplishment of common objectives.

2. Division of Work

The total work should be divided. This is known as departmentation. All the activities must be planned. This gives an idea of the total workload of the enterprise. Effective organisation must promote specialisation.

3. Span of Control

No executive in the organisation should be required to supervise more subordinates than he can effectively manage. An executive should be asked to supervise a reasonable number of subordinates.

4. Scalar Principle

Line of authority must proceed from the highest executive to the worker at the bottom level through a downward flow. This is known as 'chain of command'. The superior has a direct authority over his immediate subordinate. He is responsible for efficient performance of the work entrusted.

5. Unity of Command

Each individual should receive orders from only one boss. A person cannot serve under two masters. He is accountable to his immediate superior. Dual subordination should be avoided. It creates disorder and confusion and leads to indiscipline.

6. Functional Definition

The authority and responsibility of every individual should be clearly defined. The relationship between different jobs should be clearly specified.

7. Unity of Direction

There must be one head and one plan for a group of activities directing towards the same objectives. This is necessary to ensure completion of tasks and co-ordination of activities.

8. Co-Ordination

The various activities of undertaking should be co-ordinated to secure the desired results. The different departments may have to function frequently in close consultation with other departments in a departmental store. The purchase department and sales department activities must be well coordinated to increase profit.

9. Delegation of Authority

Delegation means the entrustment of part of the work or some duties to the subordinates. Superior has to entrust some of his duties to his immediate subordinate. The subordinates should be granted necessary powers and rights. He becomes accountable to his superior. Delegation creates obligation on the part of the subordinate.

10. The Principle of Responsibility

The superior should be held responsible for the acts of his subordinates. He cannot escape from the responsibility. He is accountable to his higher authorities.

11. Flexibility

The organization should be flexible. It should be adaptable to changing circumstances. There should be scope for expansion without disrupting the basic design.

12. Efficiency

Efficiency should be the watchword of the organisation. The organisation structure should enable the enterprise to function efficiently and accomplish its objective with the lowest possible cost.

13. Personal Ability

As people constitute an organisation there is need for proper selection, placement and training of staff. The organisation must ensure optimum use of human resources and encourage development programmes.

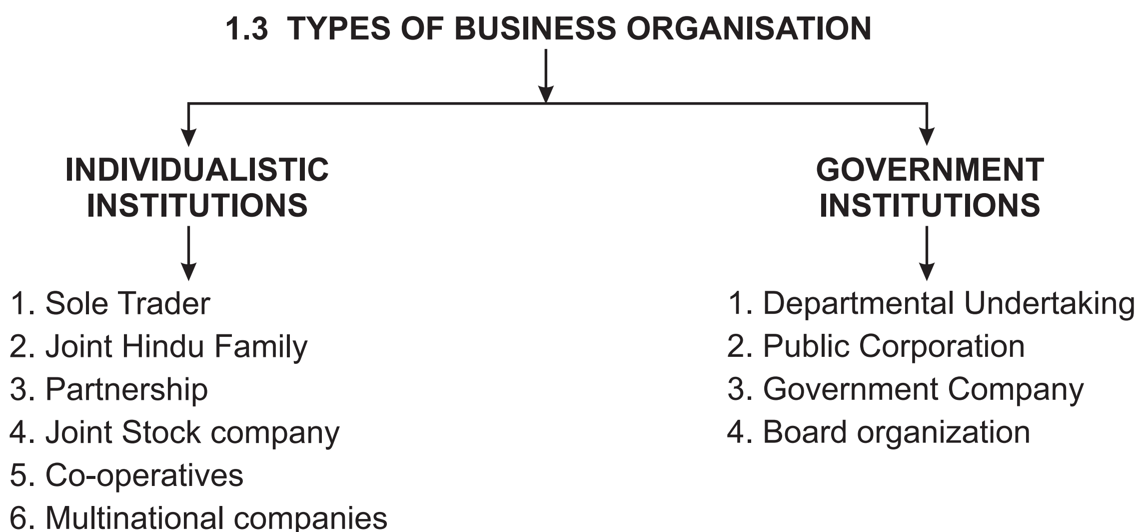
14. Simplicity

Another principle of organisation is that it should be simple. Too many levels of authority for example, complicate communication channels and by causing confusion and friction makes achievement of co-ordination impossible.

The above principles are the essential requirements for a sound organisation. In olden days, the needs and requirements of the people were very much limited. As such, the size and volume of business was at a low level. In course of time, the population increased and the demand for goods and services increased correspondingly. As a result 'Machine age' emerged resulting in large scale production. This task necessitated more investment in labour. It involved more risk. Small business concern could not face these challenges. These failures led to the establishment of corporate enterprises. On the basis of ownership, the following are the main forms of organisation. They have emerged to cope up with the needs of the people.

Since we are going to deal at length, the other forms of business organisation under separate chapters, only a very brief description of them is given below:

A Business organisation can be classified in two types, viz,. Individualistic Institutions and Government Institutions. The following chart exhibits the various types of business organisation.



INDIVIDUALISTIC INSTITUTIONS

Individualistic institutions are established by a single individual or by a number of individuals. The following are the different forms of business organisation.

1.3.1 Sole Trading Institutions

Any business unit which is owned and controlled by a single individual is known as a sole trading concern. The person who manages it, is called a sole trader. It is also named sole proprietorship business or single entrepreneurship or individual proprietorship. It is stated to be the oldest of all the forms of business enterprises. He may use his own savings for carrying on the business. He may borrow from his friends, relatives and others. He himself manages the business with an assistance from relatives or employees.

The sole trader makes all purchases and sells on his own and maintains all the account. He alone enjoys all profits and bears all losses in business. He is the founder as well as the controller of the business. The sole trading concern is run on the principle "All is he and he is all in all". It is easy to set up and manage the sole proprietor's business. No legal formalities are required.

1.3.2 Joint Hindu Family

India is unique in the system of Joint Hindu Families. A Joint Hindu Family comprises of father, mother, sons, daughters, grandsons and granddaughters. They hold the property jointly. They do the business under the control of the head of the family. These families have been engaged in occupations like agriculture, handicrafts, small industries etc. These business units are known as Joint Hindu family business. This system is found only in India.

The system of Joint Hindu family came into existence by the operation of Hindu law. There will not be any agreement among members. The firm is owned by the members of the family who have inherited their ancestral property. Their membership is conferred upon the members by virtue of their birth in the family. The head of the family is known as 'KARTA'. The members are called coparceners. It is regulated by the provisions of Hindu Law.

According to Hindu Law, a Hindu can inherit the property from three generations. In other words, a son, a grand son, a great grand son become joint

owners for the property by birth in the family. The law provides rights to women for their living and marriages in the joint family.

According to Hindu Succession Act, 1956, a coparcener will have a share in the coparcenaries property after the death of the coparcener. Since 1985, female members of the family are also eligible to get a share in the property of the family.

No Act has defined the term Joint Hindu family. However, a Jurist, while pronouncing a judgment in a case, held the view that, "A joint hindu family is a family which has the same place of worship, share the same food and share the same property of the family".

According to 'mitakshara' Law only the male members in the family get the right of inheritance by birth. It is applied throughout India except Assam and West Bengal.

According to Dayabhaga Law, the right of property devolves on the coparceners by succession and not by birth. The share in the property is not fluctuating on the basis of births and deaths. The shares are specified prior to partition. The coparceners can alienate their share of property even without the consent of their coparceners.

With the advent of industrialisation the joint families are reduced to small families. As a result, this system is declining.

1.3.3 Partnership

A sole trading concern has certain limitations. It cannot be expanded beyond a certain stage. Where large capital, and skill are necessary, a single individual cannot provide both. Two or more persons may join together and provide necessary capital and skills. Then partnership comes in to existence.

According to Prof. Haney, "Partnership is the relation existing between persons competent to make contracts who agree to carry on a lawful business in common with a view to private gain".

The partnership is formed as a result of an agreement between two or more persons. The minimum number is two and the maximum number is 10 in banking and 20 in the case of non- banking business. Partnership should not carry on any unlawful or illegal business.

Partners may share profit or loss in an agreed proportion. If there is no agreement, partners share profit or loss equally. Every partner has a right to take part in the management of the business. He has right to give his opinion. The partners are jointly and severally liable for the debts of the firm.

Persons who enter into partnership with one another are called partners. They are collectively called as a firm.

1.3.4 Joint Stock Company

A company is an association of many persons. The capital of the company is divided into small units called a share. Any one who holds or buys a share in a company is called a shareholder. Shareholders are the members of the company. A company is called a joint stock company as the capital is contributed by a large number of investors. A joint stock company may be a public company a private company.

A company is defined as, “an incorporated association which is an artificial person created by law having a common seal and perpetual succession”.

A company is considered as a person by law. It can enter into contract in its own name. It must have a common seal as it cannot sign documents. A company has continuous perpetual existence. The liability of a share holder is limited.

Shares can be freely transferred from one person to another. It encourages the people to save even small amount.

A company is an artificial person. It acquires legal entity through incorporation. Incorporation implies registration of the company with the Registrar as a body corporate. Whether it is a private company or a public company, it should be incorporated with the Registrar of companies as per the Companies Act of 1956. The management of joint stock company is entrusted to the board of directors.

1.3.5 Co-Operative Society

A co-operative society is a voluntary association of persons. Persons hailing from the same locality voluntarily join together to achieve a common economic objective. Any person can join the society. There is no compulsion to become a member of a society. A person can join a co-operative society whenever he likes and leave it whenever he wishes.

In a co-operative society all the members are equal. Every member has only one vote irrespective of the number of shares held by him. "One man one vote" is the most important principle. The society is managed on democratic principles. Every member has equal voice in the management of a society to render service to its members. Service is primary and profit is secondary.

The business of a co-operative society is generally carried on cash basis. Every state government has appointed a Registrar of co-operative societies for registering, controlling and supervising the societies. When a co-operative society is registered, it becomes a body corporate. It has separate legal existence. It is exempted from payment of stamp duty and registration fees. It also enjoys the special feature of limited liability.

1.3.6 Multinational Companies (MNC's)

The term "multinational" consists of two different words, 'multi' and 'national.' The prefix 'multi' means 'many', while the word 'national' refers to nations or countries. Therefore, a multinational company may be defined as a company that operates in several countries. Such a company has factories, branches and in more than one country. According to the United Nations Commission on Multinational Corporations, a multinational corporation is a corporation which operates, in addition to the country in which it is incorporated, in one or more other countries.

A multinational corporation is also known as a transnational corporation, namely, 'Global giant', or 'World enterprise' or 'international enterprise'. All forms of business organisation that transcend political frontiers may be called as multinational firms.

In simple words, a multinational company is a company carrying on business in two or more countries. According to Neil H.Jocoby "A multinational corporation owns and manages business in two or more countries"

FEATURES

1. A multinational company is operated in more than one country simultaneously.
2. It is generally very large in size.
3. Its purpose is to reduce transport costs and to make use of raw materials, labour, capital and market of foreign countries.

There are 500 to 700 MNCs operating in the world today, half of them are U.S multinationals and the rest are based outside United States. The multinationals based in the USA have the largest share of foreign direct investment, followed by the U.K, Germany, Japan, Switzerland, France and Canada. In underdeveloped countries the investment and employment created by the MNCs have been chiefly concentrated in about a dozen nations, namely, Brazil, Mexico, Hong Kong, Philippines, Singapore and South Korea. According to the study of International Labour Organisation (ILO) Latin America accounts for about 60% of the MNC employment in developing countries, followed by Asia 30% and Africa 10%. Foreign investment has moved to a limited number of developing countries which offer political stability and a convenient economic environment, including tax incentives, large markets, cheap labour and easy access to oil and other natural resources.

Examples

A few examples of multinational companies are given below:

1. Unilever Limited

It is a British company that has subsidiaries and branches in several countries. It established a subsidiary company called Hindustan Lever Limited in India.

2. Union Carbide

It is an American company, which has plants and subsidiaries in several countries including India.

3. International Business Machine (IBM)

It is an American company having branches in several countries.

4. Philips

It is a Dutch Company having a subsidiary company called Philips India (Now Pieco Electricals Co) in India.

5. Coca Cola Corporation

It is an American company manufacturing and selling soft drinks in several countries.

According to Peter Drucker, there is a good feature for MNCs in the coming years. Govt. policy is also favourable towards multinationals. On account of the economic reforms made by the Government MNCs are going to be benefited. Inviting foreign capital, automatic clearance will help the MNC's to grow and develop in India.

GOVERNMENT INSTITUTIONS

In the present age, in order to expedite the economic progress of the country the government also establishes and conducts business.

Public sector enterprises are those enterprises which are owned, controlled and operated by the central or state government or by both. Such enterprises are run mainly to provide service to the public. The performance of public enterprises is discussed in the parliament. These enterprises are generally established as semi-autonomous or autonomous bodies. They are engaged in industrial and commercial activities.

In India, the central and state governments have established several public enterprises. These enterprises produce a wide variety of goods such as iron and steel electronics, ships, aircrafts, locomotives, heavy machinery, fertilisers, chemicals, insecticides, drugs and consumer products. Many of the public enterprises are very large in size employing thousands of workers and having investment of several hundred crores of rupees.

1. Departmental Undertaking

This is considered as a department attached to the ministry of a government. Its administration is in the hands of the chief administrative officer of the ministry. Here the department is a part of the government. This is the oldest form of

organisation of state enterprise. It may be run either by central government or by the state government. Railways, B.S.N.L.,(telephones) Broad castings like Doodharsan are the examples of Departmental Undertakings.

2. Public Corporation

This is established under a specific statute passed in the parliament. It is known as a statutory corporation because it is created by a statute. The statute defines its objectives, powers and functions. It is an autonomous body fully financed by the government. It has a separate legal existence independent of the government. The corporation is wholly owned by the government. Its entire share capital is contributed by the state. Its management is vested with a Board of Directors appointed or nominated by the government. There is no government interference in the day to day working of the corporation. The main object of the corporation is to serve the public. A statutory corporation has its own staff. Its employees are not government servants. It is fully accountable to the parliament or state legislature. Reserve Bank of India, Life Insurance Corporation and Unit Trust of India are the examples of public corporation.

3. Government Company

Government Company is also established under the Companies Act of 1956. It is a company in which not less than 51% of paid up share capital is held by the central government or by one or more state governments or jointly by the central and state governments. In India the Government Companies also subscribe share capital of the Private Company and so sometimes it is known as mixed ownership company. It is a body corporate independent of the government. It is managed by a Board of Directors nominated by the government and other shareholders. Its employees are not Government servants. They are not governed by civil service rules. It enjoys borrowing powers. It is accountable to the ministry or department concerned. Hindutan Steel Limited, Bharath Heavy Electricals Limited, Maruthi Udyog are the examples of Government Company.

4. Board Organisation

In this organisation management is carried on by a government nominated independent Board. It has its own rules and regulations. Tamil Nadu Electricity Board, Tamil Nadu Housing Board, TamilNadu Water and Drainage Board are the examples of Board Organisation.

Comparative study of Different Forms of Business Organisation

Basis of Comparison	Sole Proprietorship	Joint Hindu family firm	Patnership firm	Private Ltd. company	Public Ltd company	Cooperative organisation
1	2	3	4	5	6	7
1. Regulating Act	No	Hindu Law & Hindu Succes sion Act1956	Indian Parnetership Act 1932	Companies Act 1956	Companies Act, 1956	Cooperative Societies Act 1912 or the State Coopera tive Act.
2. Membership	Single	No.of Male members	Minimum-2 Maximum-10 in banking & 20 in others	Minimum-2 Maximum-50	Minimum-7 Maximum - No Limit	Minimum-25 Maximum - No Limit
3. Separate Legal Entity	No	No	No	Yes	Yes	Yes
4. Members Liability	Unlimited	Karta-unlimited Others Limited	Unlimited	Limited	Limited	Limited
5. Continuity of business	Unstable, Terminates with the death, insolvency or lunacy of the owner	Stable,Comes to end only when all the coparceners die or partition is demanded by one of them	Less stable May be dissolved by death or insolvency of any parnter	Perpetual Existence, Life not affected by the death of any member	Long Life	Long Life

1	2	3	4	5	6	7
6. Legal Formalities in formation	No	No	Less	Much	More	Much
7. Origin	By individual	By birth of members. (Operation of Law)	By agreement	By incorporation	By incorporation	By incorporation
8. Registration	NotNecessary	Not Necessary	Optional	Compulsory	Compulsory	Compulsory
9. Financial Requirements and Suitability	Less Capital, suitable for small business	Less Capital, suitable for small business	More capital, Suitable for medium scale business	Large, suitable for medium scale business	Very large, suitable for large scale business	Less requirement, suitable for small & medium scale business
10. Divorce between ownership & management	No	No	No	Less	Generally More	Less
11. Transferability of Interest	At will	Restricted	Restricted	Restricted	At will	Restricted

1	2	3	4	5	6	7
12. Basis of profit sharing	Full	Equal	Agreement	No.of Shares held	No.of Shares held	Volume of business of each member
13. Compulsory audit	No	No	No	Yes	Yes	Yes
14. State regulation	Practically none	Practically none	Limited	Considerable	Excessive control	Considerable
15. Winding-up	At will	At will	Under the Act	Under the Act	Under the Act	Under the Act

POINTS TO REMEMBER

Business organisation may be defined as "harmonious combination of the parts of factors of a business for the purpose of producing or acquiring wealth"

❖ **Principles of organisation**

1. Unity of objectives 2. Division of work 3. Span of control 4. Scalar principle 5. Unity of command 6. Functional definition 7. Unity of direction 8.Co-ordination 9.Delegation of authority 10. The principle of responsibility 11. Flexibility 12. Efficiency 13. Personal ability 14. Simplicity

❖ **Various froms of business organisation**

1. Sole trader 2. Joint-hindu family 3. Partnership 4. Joint Stock Company 5. Co-operation 6.Multinational companies 7. Departmental undertakings 8. Public Corporation. 9. Government Company 10. Board organisation

❖ **Comparative study of Different forms of Business organisation**

1. Act 2.Membership 3. Separate legal entity 4. liability 5. Continuity 6. legal formation 7. Registration 8. Finance suitability 9. Origin 10. Separation of ownership 11. Transferability of interest 12. Basis of profit sharing 13. Audit 14. State regulation 15. Winding up

QUESTIONS

I. Indicate the correct answers.

1. Which of the following is not the characteristic of sole proprietorship

   a. Single ownership

   b. One man control

   c. Whole profit to proprietorship

   d. Non-flexibility **Ans: (d)**

2. What is the advantage of sole proprietorship

   a. Small capital

   b. Hasty decision

   c. Limited capital

   d. Limited managerial ability **Ans: (c)**

3. The agreement of partnership

    a. Must be oral

    b. Must be in writing

    c. Must be writing in the stamp paper

    d. Can be either oral or in writing **Ans: (c)**

4. Partnership may come into existence

    a. By the operation of law

    b. By an express agreement

    c. By an express or implied agreement

    d. By inheritance of property **Ans: (b)**

5. Management of a Jointstock company is entrusted to.

    a. The Registrar of companies

    b. The Board of Directors

    c. The shareholder

    d. The debenture holders **Ans: (b)**

6. Registration is compulsory in the case of

    a. A Sole trader

    b. A partnership

    c. A joint stock company

    d. A joint hindu family business **Ans: (c)**

7. In a co-operative society

    a. One share one vote principle is followed

    b. One man one vote principle is followed

    c. A member must have 2 votes

    d. Shares are transferable. **Ans: (b)**

8. Co-operative society can be started

   a. Only in villages

   b. In towns and villages

   c. Only in cities

   d. Only in State headquarters **Ans: (b)**

9. The most suitable form of organisation for operating defence industries is

   a. Government Company

   b. Public corporation

   c. Departmental organisation

   d. Board organization **Ans: (c)**

10. The share capital of the government company must not be less than

    a. 75%

    b. 60%

    c. 95%

    d. 51% **Ans: (d)**

11. A multinational company is also known as

    a. Global giant

    b. Partnership

    c. Co-operative society

    d. Public corporation **Ans: (a)**

12. Membership by birth is main feature in

    a. Sole trader

    b. Joint Hindu family business

    c. Co-operative society

    d. Partnership **Ans: (b)**

II. Fill in the blanks

1. Division of work is called ______________

2. Delegation means the ________________ of part of the work

3. The liability of sole trader is ________________

4. Partners share profits and losses ____________

5. In India registration of partnership is ___________

6. In co-operative society all members are ____________

7. A company is regarded as a _____________

8. Broadcasting comes under ___________ form of organization

9. Public corporation is known as _________ corporation

10. Tamilnadu Electricity Board is the example of _____________

11. Government policy is also favourable towards ____________

12. Government Company employees are not _______________

(Ans)

1.	Departmentation	7.	person by law
2.	Entrustment	8.	Departmental
3.	Unlimited	9.	Statutory
4.	In an agreed ratio	10.	Board organization
5.	Optional	11.	Multinationals
6.	Equal	12.	Government servants.

III. MATCH THE FOLLOWING

1.	Departmentation	a.	Chain store
2.	Joint hindu family business	b.	Grouping of activities
3.	Joint Stock Company	c.	KARTA
4.	Co-operative society	d.	Separate legal existence
5.	Sole trader	e.	Dividend based on purchase
6.	Public Undertakings	f.	Absence of the benefit of collective Judgement
		g.	Government Ownership

(Ans) (1.b; 2.c; 3.d; 4.e; 5.f; 6.g;)

IV. Short Questions

(Answer should not exceed 5 lines)

1. Define organisation
2. What is scalar principle?
3. What do you mean by co-ordination?
4. What is sole trading business?
5. Explain the term ‘partnership’
6. Who is a KARTA?
7. What do you understand by co-operation?
8. What is public corporation?
9. State the meaning of Board organisation
10. Give five examples of Multinational companies

V. Paragraph Questions.

(Answer should not exceed one page)

1. Write short notes on Joint hindu family business
2. Explain any two types of individualistic institutions
3. Does partnership remove all the defects of sole proprietorship?
4. On what reasons study of organisation is important?

VI. Essay Type Questions

(Answer should not exceed 3 pages of normal handwriting.)

1. Explain briefly the principles of organisation.
2. Describe the various types of business organisation.
3. What do you understand by multinational companies and explain its features.

CHAPTER - 2
SOLE TRADER

" Business is like riding a bicycle;

either you keep moving or you fall down".

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 2.1. Main Forms of Non-Corporate Enterprises.
- ❖ 2.2. Meaning and Definition of Sole trader.
- ❖ 2.3. Characteristics of Sole proprietorship.
- ❖ 2.4. Merits of Sole proprietorship.
- ❖ 2.5. Demerits of Sole proprietorship.
- ❖ 2.6. Business for which Sole proprietorship is suitable.
- ❖ 2.7. Role of sole proprietorship in the Society.
- ❖ 2.8. One-man control is the best in the world.

2.1 MAIN FORMS OF NON-CORPORATE ENTERPRISES

Forms of business organisation can be divided into two main types on the basis of ownership viz., corporate form and non - corporate form. In the corporate form, the legal entity of the enterprise is distinct from that of its owners ie., the ownership is separated from its management and the owners cannot take direct control over the business.

But in a non-corporate form, the enterprise and its owners are considered as having the same entity ie., the ownership and business are not separated. Owners can have direct control over business. Non-corporate business may be organised

either as a sole proprietorship or as a partnership or as a joint hindu family business. In this chapter the meaning ,features, merits,demerits,suitability and social responsibility of sole trader business are discussed in detail.

2.2 MEANING

A sole tradership is the oldest form of business organisation. It is easy and simple to organise. It is found in each and every country in the world. This type of organisation has not lost its utility even today. Sole proprietorship is a form of organisation in which an individual invests the entire capital, uses his own skill and is solely responsible for the result of his business. He may borrow money and employ assistants. But he alone owns and controls the business and bears its profit and loss. The only legal formality is to get a licence from the local authority viz, municipality, panchayat etc., for running certain type of business. It is also known as individual proprietorship or one-man business. The person who contributes capital and manages the business is called as sole trader or sole proprietor.

DEFINITION

1. According to P.K. Ghosh and Y.K. Bhushan, “The sole proprietorship is a form of organisation in which an individual introduces his own capital, uses his own skill and intelligence, and is entirely responsible for the results of its operations”.

2. Dr.O.R.Krishnaswami has defined the sole trader form of organisation as "a business carried on by a single person exclusively by and for himself ".

3. Encyclopedia of Business and Commerce defines sole trading concern as, “ a form of organisation, in which an individual alone invests his capital, uses his own skill and intelligence in the management of its affairs and is entitled to enjoy all the profits as also is solely responsible for all the risks of ownership”.

4. According to Wheeler, “ the sole proprietorship is that form of business organisation which is owned and controlled by a single individual. He receives all the profits and risks all of his property in the success or failure of the enterprise”.

5. In the words of James Stephenson, “A sole proprietor is a person who carries on business exclusively by and for him… He is not only the owner of the capital of the undertaking, but is usually the organiser and manager and takes all the profits or responsibility for losses”.

2.3 FEATURES

The salient features of a sole trading concern are as follows.

1. One-man Ownership and Control

A sole trading concern is owned by an individual. The proprietor is the sole

owner and master of the business. He independently manages and controls the business without the interference of any other person.

2. Capital Contribution

In sole tradership, the capital is employed by the owner himself from his personal resources. He may also borrow capital from his friends, relatives and financial institutions.

3. Unlimited Liability

The liability of the proprietor for the debts of the business is unlimited. The creditors have the right to recover their dues even from the personal property of the proprietor in case the business assets are not sufficient to pay their debts.

4. Enjoyment of Entire Profit

The sole trader is entitled to enjoy all profits of the business. Since he is the only person who invested money, he need not share the profit with anybody else. At the same time, he himself should bear the entire loss. So it is said that he owns all and risks all.

5. No Separate Legal Entity

The sole trader and the business are one and the same. A sole trading concern has no legal entity separate from its owner.The sole trader owns the assets and owes the liabilities of the concern.

6. No Special Legislation

Sole tradership is not governed by any special legislation. A partnership firm is governed by the Indian Partnership Act. A joint stock company is governed by the Indian Companies Act and a co-operative society by the Co-operative Societies Act. But soletrader business is not governed by any Act.

7. Registration

A soletrader business need not be registered with any authority as that of partnership and companies. Any person who has money can start the sole trader business. He is to obtain a licence from the local authority like municipality or panchayat.

8. Duration

The life of sole trader business depends upon the life of the soletrader. If he dies or becomes incapable of doing business or if he has no legal heir, the business comes to an end.

9. Simplicity

It is simple to commence and simple to close a sole trader business. It requires lesser efforts and it is free from complicated legal formalities.

10. Local business

Most of the sole trading business confine only to a particular place such as a street, a block or a village. A few sole trading business may cover a large area through a network of a branches.

11. Self Employment

A sole trader uses his own labour to conduct the business. He may employ a few paid servant or use the services of his family members for running the business.

12. Small Capital

A soletrader business can be commenced with a small amount of capital whereas a partnership firm or a company require large capital.

2.4. MERITS

The advantages of a sole trading concern are as follows.

1. Easy Formation

Sole proprietorship is the only form of organisation where no legal formalities is required. No agreement is required and registration of the firm is not essential. Anybody willing to start a sole-trading concern can do so immediately and without much legal formalities.

2. Direct Motivation

The entire profit of the business goes to the sole trader. Nobody can claim a share in the profit. It motivates him to expand his business activities.

3. Flexibility

It is a highly flexible type of organization. A sole proprietorship concern is generally run on a small scale basis. In case a change in operation is required, it is possible without involving much expenditure. The proprietor can adapt and adjust the activities of the business to the changing trends and market conditions because the sole trader is the sole owner of his business.

4. Retention of Business Secrets

The maintenance of utmost secrecy is of vital importance for the success of a business. A soletrader can maintain business secrets. Being the sole proprietor, he is not expected to share his trade secrets with anybodyelse. In this form of organisation, there is also no need to disclose accounts or any other material facts to the public.

5. Quick Decision

The sole proprietor is his own boss and need not consult others while making any decision. He exercises exclusive control over the affairs of the business. Therefore, he can take quick decision and implement them without any delay.

6. Higher reward

The fear of loss acts as a stimulant for hard work. Besides, it makes him very cautious in his approach. Hardwork and cautious approach bring him more reward and improves efficiency and economy of the business.

7. Effective Control

In this form of organisation, the business can be controlled effectively because business activites are planned and executed by a single man. Since all the decisions relating to purchase and sale are taken by the soletrader, he can effectively control the business if there is any deviation from the original plan.

8. Increase in Sales

A sole trader has direct relationship with the customers. Direct contact with the customers will enable the proprietor to know the nature of their tastes, likes and dislikes. It enables him to make necessary changes in the quality and design of his products. It will boost his sales besides enhancing the reputation of the firm.

9. Smooth running of Business

Since the sole trading concern is a small business the soletrader appoints only a few employees who are personally known to him. So he can understand their problems easily and able to solve them to their satisfaction. The absence of friction with the employees paves the way for the smooth running of the business.

10. Inexpensive management

The soletrader is the owner, manager and controller of the business. He does not appoint specialists for various functions. He personally supervises various activities and can avoid wastage in the business. In this way managerial expenses are reduced to a large extent.

11. Higher Credit Rating

The liability of a sole trader is unlimited. Since, apart from his business assets, even his private properties are also available for satisfying the claims of creditors. Hence, creditors may give more loans because they can get back the loan from the personal properties of soletraders. Thus high credit rating helps soletrader to borrow more funds from suppliers and banks.

12. Self-Employment

Sole proprietorship provides self employment opportunity to many persons with small resources. It offers a way of life for securing the means of livelihood to those who do not want to serve under others. It makes people self-dependent by providing self- employment.

13. Development of Personality

Sole proprietorship facilitates the development of personal qualities like self-reliance, initiative and independent judgement.

14. Equal Distribution of Economic Wealth

Sole proprietorship provides an equal opportunity to every one for self development. It promotes decentralisation of business and helps to avoid concentration of economic wealth in a few hands.

15. Easy dissolution

A sole trading concern is very easy to dissolve. Whenever a sole trader wants to close his business, he can do so without undergoing any legal formality.

16. Better co-ordination

As the size of the business is small with limited resources, the sole trader can effectively co-ordinate the activities of the business.

2.5.I. DEMERITS

1. Limited capital

The resources of a sole proprietor are limited. He depends only on his personal resources and his borrowing capacity. The borrowing capacity depends on his assets and credit worthiness. It is obvious that financial resources of a single person will be insufficient for business expansion. Limitation of finance is a major handicap for sole-trader business. Therefore, the size of the firm remains small.

2. Limited Managerial Ability

The managerial ability of a soletrader is limited because a person may not be an expert in each and every field of business such as purchasing, selling, accounting etc. The sole proprietor may not be able to use the service of experts for want of resources. The limited managerial capacity may hinder the growth of the business.

3. Unlimited Liability

The unlimited liability of a sole proprietor may affect his enthusiasm and restrict introducing novel ideas in business.

4. Short Life

Anything which affects the personal life of a soletrader affects his business also. Prolonged illness or death of the soletrader brings the affairs of his business to a stand- still. If his children are interested and efficient to run the business, the sole trader business can be continued. Otherwise it will be closed. The closure of a business will cause inconvenience to the consumers and may also result in social loss.

5. Hasty Decisions

Decisions arrived at, after deep deliberations and discussions are sure to be better than that of a decision taken by one man. It is rightly said two heads are always better than one. The chances of wrong decision-making are quite high in a sole trader business. This is because of the fact that the sole trader takes all decision of the business himself without any assistance. This may lead to wrong decisions. The hasty decisions may result in loss and affect the sole trader.

6. Lack of Specialisation

The sole trader has to undertake all the work relating to business himself such as buying, selling, accounting, financing, advertising etc. He is a jack of all trades but master of none. It would be difficult to avail the services of experts in his business because of small resources. So, the benefits of division of labour cannot be reaped and specailisation cannot be achieved in this type of business.

7. Uneconomic Size

Because of limited capital and skill, the sole traders have to work on a small scale basis. Thus he is deprived of economies of large scale operation.

8. Lack of Consultation

He has no one else to consult before taking any important decisions except his family members. This may result in heavy loss if his decisions go wrong.

9. Uncertainty

The life of the sole trader business is uncertain and unstable. The life of business depends upon the changes in taste and preferences of customers and changes in fashion and technology. If soletrader fails to cope up with the latest development he will land in trouble.

10. Risk of Entire Loss

As the sole trader is the sole owner of the business, he has to bear all losses of his business.

2.6. SUITABILITY

Sole proprietorship is suitable for the following business:

1) Where small amount of capital is required,

   e.g., Sweet shops, Bakery shops, Petty shops, etc,

2) Where quick decisions are very important,

   e.g., Share-brokers, Doctors, etc.

3) Where limited risk is involved,

   e.g., Automobile repair shops, Small retail stores, etc.

4) Where personal attention to individual tastes and fashions of customers is required,

   e.g., Beauty parlours, Tailoring shops, etc.

5) Where the demand is local, seasonal or temporary,

   e.g., Retail trade, Laundry, Fruit sellers, etc.

2.7. ROLE OF SOLE PROPRIETORSHIP IN THE SOCIETY

Consumers are the kings. They decide the success of a business. Their needs, desires, expectations are to be satisfied by the businessmen. Sole proprietorship occupies a pivotal role in satisfying the multifarious needs of consumers regarding goods and services. The day to day requirements of the consumers such as food items, cloth, stationaries, laundries, provisions, books and newspapers, medicines etc., are supplied by the soletrader form of organisation. The soletrader who supply these goods are respected by the society. Thus the soletraders have a responsibility to promote the welfare of the society. Sole proprietorship has its own areas of activity and continues to exist inspite of the development of bigger organisations. This form of organisation has a social desirability also. It provides valuable services to the society. Its social necessity arises due to the following ways.

1. Solution to unemployment problem

Sole trader business organisation gives large employment opportunities to the less educated and uneducated persons and helps to reduce the unemployment problem in the society.

2. Provides Investment Avenues

Soletrader organisation provides a chance for small investors who has small amount of capital to utilise their savings in the productive line.

3. Provision of goods at low price

Goods are sold by soletraders at a price lesser than the maximum retail price (MRP) mentioned on the packages of the goods. This is possible due to inexpensive management.

4. Helps small producers

Most of the goods sold by soletraders are procured locally from local producers. Thus small local producers are benefited by the soletraders.

5. Supply of Quality goods

Soletraders sell goods of high quality nowadays to maintain their reputation. They even accept return of defective goods. This ensures enhancing the welfare of the public.

6. Philanthrophic Activities

Soletraders form small trading organisation among themselves and undertake a number of social welfare activities such as conducting eye camps, maintaining parks, provision of baricades on the roads, supplying furnitures to schools etc.

7. Equal Distribution of Income and Wealth

Equal distribution of income and wealth is ensured as there are more entry of sole proprietors in trading activities.

8. Helpful to consumers

The soletraders supply the goods to the consumers at their door steps. So the time and energy of the consumers are saved.

2.8. ONE-MAN CONTROL IS THE BEST IN THE WORLD

William R. Basset has said that one-man control is the best in the world only when the business is small indeed, to allow one actually to know and supervise everything in the business.

Following are some of the points in favour of one man control

1. Easy and quick formation.
2. Direct control.
3. Efforts and reward are linked.
4. Retaining business secrets.
5. Close touch with the consumers.

6. Enjoying all profits.
7. Inexpensive management.
8. No legal restrictions.
9. Direct contact with the employees.
10. Social desirability.

Limitations of one-man control

Though there are many advantages of one-man control, still it suffers from many drawbacks. One man is unable to manage all the affairs by himself. Basset says " The danger is always present that he thinks, he knows which really he does not know". Following are some points unfavourable for one-man control.

1. Limited capital.
2. Limited managerial ability.
3. Unlimited liability.
4. Absence of large scale business operation.
5. Risky decisions.
6. Uncertainty.

In conclusion, one-man control is the best from the point of view of profitability and efficiency, provided that one man is able to manage everything efficiently.

Points to Remember

❖ **Meaning and nature**

The sole trading concern is the simplest and oldest form of organisation. A soletrader is one who carries on business exclusively by or for himself.

❖ **Features**

1. One man Ownership and control 2. Capital contribution 3.Unlimited liability 4. Enjoyment of Entire profit 5. No Separate legal entity 6. No special legislation 7. Registration 8.Duration 9.Simplicity 10.Local business, 11. Self employment 12. Small capital.

❖ **Merits**

1.Easy formation 2. Direct Motivation 3.Flexibility 4. Retention of business secrets 5. Quick decision 6. Higher reward 7. Effective control 8. Increase in Sales 9. Smooth running of business 10.Inexpensive management 11. Higher Credit rating

12. Self- employment. 13 Development of personality 14. Equal distribution of economic wealth 15. Easy dissolution 16. Better co-ordination.

❖ **Demerits**

1. Limited capital 2. Limited managerial ability 3. Unlimited liability 4. Short life 5. Hasty Decisions 6. Lack of specialization 7. Uneconomic size 8. Lack of consultations 9. Uncertainty 10. Risk of entire loss.

QUESTIONS

A. Objective Type

I . Multiple Choice

1. Sole trading business can be started by:
   a) At least two persons
   b) At least seven persons
   c) Any one person
2. The liability of a soletrader is:
   a) Limited only to his investment in the business
   b) Limited to total property of the business
   c) Unlimited
3. Sole proprietorship is suitable for:
   a) Large scale concerns
   b) Medium scale concerns
   c) Small scale concerns
4. Decision-making process in soletrading business is:
   a) Quick
   b) Slow
   c) Neither quick nor slow
5. A soletrader:
   a) Cannot keep his business secrets
   b) Can keep his business secrets
   c) None of the above

Ans. 1.(c)., 2. (c)., 3. (c)., 4. (a)., 5. (b).

II. Say " True " or " False " to the following statements

1) A sole trader has a limited liability.

2) Sole proprietorship is the oldest from of organisation.

3) It is not difficult to form a sole-trading business.

4) No legal formality is required to start a sole trading business.

Ans. True ; (2) ; (3) ;(4);

False; (1).

B. Short Questions

(1) State the various kinds of non-corporate enterprises.

(2) What is a sole proprietorship business?

(3) Define “sole trader”.

(4) What is unlimited liability?

C. Essay type questions

(1) Explain the main characteristics of sole trading form of organisation.

(2) Discuss the merits and demerits of sole trading form of business.

(3) Explain the role of soletrading concern in the society.

(4) "One man control is the best in the world provided that one man is big enough to take care of everything” Discuss.

CHAPTER - 3
PARTNERSHIP

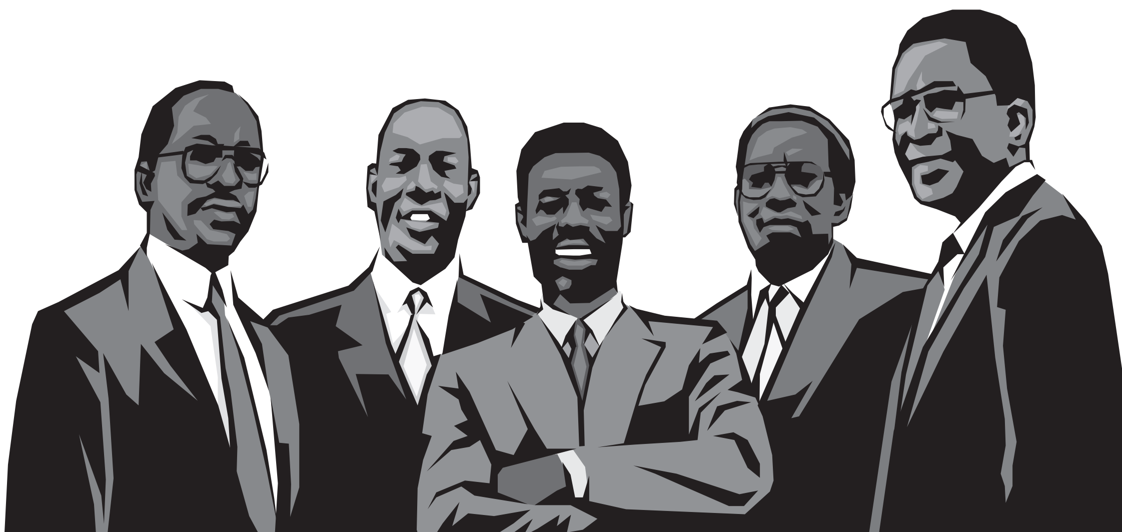
Coming together is a beginning

Keeping together is progress

Working together is success.

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 3.1. Meaning and definition of partnership.
- ❖ 3.2. Essential features of partnership.
- ❖ 3.3. Comparison between sole tradership and partnership.
- ❖ 3.4. Merits and demerits of partnership.
- ❖ 3.5. Types of partnership.
- ❖ 3.6. Kinds of partners.
- ❖ 3.7. Rights, duties and liabilities of partners.
- ❖ 3.8. Partner's express and implied authority.
- ❖ 3.9. Partnership deed, meaning and contents.
- ❖ 3.10.Procedure for the registration of firm.
- ❖ 3.11. Modes of dissolution of partnership firm.



INTRODUCTION

The need for partnership form of organisation arose from the limitations of sole proprietorship. In sole proprietorship, financial resources and managerial skills are limited. One man cannot supervise personally all the business activities. Moreover, risk - bearing capacity of an individual is also limited. It is at this stage that a need for associating more persons arises. So more persons are associated to form groups to carry on business.

The partnership form of organisation comes into existence in two ways. It may come into existence either as a result of expansion of the sole trading concern or two or more persons joining together through an agreement to form a partnership. In otherwords, it is an extension of sole trading concern.

History reveals that the partnership organisation was started with the enactment of Partnership Act in 1907 in England. In India, the Act was approved in 1932. The Act governs the formation, management and control of various partnership firms in the country. A number of partnership enterprises are seen in market today. Examples of partnership firms are: running a cinema theatre, a book shop, chit funds etc.

3.1 DEFINITION OF PARTNERSHIP

According to the Section 4 of Indian Partnership Act of 1932, partnership is "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all".

In the words of Prof. Haney, "partnership is the relation existing between persons, competent to make contracts, who have agreed to carry on a lawful business in common with a view to private gain".

According to Dr. William R.Spriegel, "partnership has two or more members, each of whom is responsible for obligation of the partnership. Each of the partners may bind the others and the assets of partners may be taken for the debts of the partnership".

In the words of Kimball and Kimball, "A partnership or firm as it is often called, is thus a group of men who have joined capital or services for the prosecuting of some business".

Partnership may be defined as, "that form of business organisation in which, partners agree to share the profits of a lawful business , managed and carried on either by all or by any one of them acting for all".

Partner, Firm and Firm Name

Persons who enter into partnership are individually called "Partners" and collectively called "a firm" and the name under which the business is carried on is called "firm name".

3.2 FEATURES OF PARTNERSHIP

The following are the main features of partnership firm.

1.Agreement

A partnership is created by an agreement. The agreement may be oral or in writing. It is better to put it in writing to avoid misunderstanding in future.

2. Multiplicity of Person

Partnership is the relationship between two or more persons. So, there must be more than one person. The maximum number of partners has been limited to 10 in the case of banking business and 20 in the case of other business.

3. Contractual Relation

The relation that exists between the partners in a partnership is said to be contractual and not natural relation arising out of mutual love and affection. According to Indian Partnership Act, "the relation of partnership arises from contract and not from status". Only persons legally capable of making an agreement can become partners. Lunatics, insolvents cannot become a partner.

4. Lawful Business

Partnership is formed to do a business. Business means any trade or occupation or profession. [E.g., Partnership of chartered accountants, partnership of lawyers, general stores etc.,] The business must be legal i.e., not against any law in force in the country. A partnership to smuggle goods from one country to another is illegal.

5. Sharing of Profits

The profit or loss of partnership is shared by the partners in the ratio as given in the agreement. Normally profit or loss is shared according to the capital contribution of partners. But sometimes the partners may agree that a particular partner need not share any loss. If there is no agreement regarding sharing of profit or loss, all the partners share equally.

6. Agency Relationship

There must be agent and principal relationship between the partners. Every partner is a proprietor as well as an agent of the firm. The business of the firm may be carried on by all or any of them acting for all. Partnership is, therefore, described as an extension of the 'Principle of Agency'.

7. Unlimited Liability

The liability of partners is unlimited. Each and every partner has unlimited liability for business debts. If the assets of partnership are not sufficient to repay

all the business debts in full, the private assets of all the partners can be used to settle the debts. Therefore, a partner's liability for business debts is not limited to his contributed capital. But the unlimited liability of a partner is also joint and several.

8. Joint and Several Liability

The liability of partners is joint and several. The creditors of partnership firm can claim their dues from the private assets of all the partners taken together or they can take action against the private properties of any one of the partners to get back their dues

9. No Separate Legal Entity

A partnership firm has no separate legal entity. The firm and the partners are one and the same. A collective name of partners is known as "firm". No firm can exists without partners. The rights and liabilities of the partners are the rights and liabilities of the firm. Management and control of the firm vests with the partners who are also the owners.

10. Implied Agency

Each and every partner is considered to be an agent of the business. Unless otherwise agreed, all the partners are entitled to take part in the management of the business. Every partner as an agent can bind the firm by his acts done in good faith and on behalf of the firm. This is known as the implied authority of partnership.

11. Utmost Good Faith

The basis of partnership business is good faith and mutual trust among the partners. Each and every partner should act honestly and faithfully in the conduct of business. They must render true account and complete information regarding the conduct of the business. No partner can make any secret profit. Distrust and suspicion among the partners may lead to the failure of firms.

12. Non-Transferability of Interest

No partner can transfer his interest or sell his share to any other person without the consent of all other partners. This is based on the principle that a partner, being an agent himself, cannot further delegate his authority unilaterally to others.

13. Registration

In India the registration of partnership firm is not compulsory. It is only optional. If it is registered, it can enjoy certain advantages. A firm can be registered at any time.

3.3. COMPARISON BETWEEN SOLE TRADERSHIP AND PARTNERSHIP ORGANISATION.

1. Similarities: The following are the similarities of sole trader and partnership organisation.

1. **Easy formation** : Both the business are easy to establish.
2. **Flexibility** : Both the business can be altered if they are unsuccessful.
3. **No permanent existence** : Both the business suffer from short life.
4. **Unlimited liability** : The liability of sole trader and partners are unlimited.
5. **Size of business** : The size of both the business is smaller.
6. **Government control** : Interference of government is almost nil in both the business.
7. **No compulsory audit** : Audit of accounts is not compulsory for both.
8. **Personal attention** : Sole traders and partners can give personal attention for running the business.
9. **Direct touch with the customers** : Owners can have direct touch with the customers.
10. **Personal contact with employees** : Direct supervision of employees is possible in both the business
11. **Ownership and control** : It rests with owners in both cases.
12. **Registration is not required** : Registration of the business is not compulsory for both.

2. Differences between Partnership and Sole Trader.

S.No	Basis of Differences	Partnership	Sole trader
1	Specific Act	The partnership firm is governed by the Indian Partnership Act, 1932	There is no separate act for sole trader business.
2	Number of Members	Minimum 2. Maximum 10 for banking business and 20 for other business.	Only one person.
3	Agreement	Agreement is essential which may be oral or in writing	No agreement is necessary.

(1)	(2)	(3)	(4)
4	Registration	Optional	Need not be registered
5	Ownership and control	Lies with the partners	Lies with the sole proprietor.
6	Management	All partners can participate in the management.	This business is managed by one person only.
7	Capital	All the partners contribute capital.	The sole trader contributes the entire capital
8	Liability	Joint and several liability	Unlimited liability
9	Implied agency	Generally every partner is an implied agent of the firm and other partners.	The proprietor may appoint an agent.
10	Division of profit or loss	Partners share profit or loss in an agreed ratio.	The profit or loss is borne by the sole trader.
11	Decision-making	It may be delayed as all the partners must agree to the important decisions	It is very quick as the individual is not required to consult others.
12	Division of work	The partners divide the work among themselves.	No division of work
13	Secrecy	Secrecy cannot be maintained as it is open to all the partners.	Secrecy can be maintained.
14	Economic strength	It is economically more strong.	It is economically weak.
15	Survival	Its chance of survival is greater	Its chance of survival is limited.

3.4 ADVANTAGES

The following are the advantages of partnership form of organisation.

1. Easy Formation.

A partnership firm is very easy to form. No formal documents is required to be prepared as necessary in the case of joint stock company. A simple agreement among the partners is sufficient to start a partnership firm.

2. Registration not compulsory

A partnership firm is relieved of registration because registration is not compulsory. It is left to the discretion of the partners.

3. Larger Financial Resources

As a number of partners contribute to the capital of the firm, it is possible to collect larger financial resources than the sole proprietorship. Creditworthiness of the firm is also higher because every partner is personally and jointly liable for the debts of the business. Larger resources gives greater scope for the expansion of business.

4. Greater Managerial Talent

The partners may be assigned duties according to their talent. Different functional departments may be managed and controlled by different partners. The talent and experience of partners will help to increase the efficiency of the business resulting in more profit.

5. More Credit Standing

The partners may have sufficient contacts in the market. They can offer more guarantees to the financial institutions to obtain loans. The liability of partners being unlimited, they will be able to raise more finance. As compared to sole trading business, partnership concern has more credit worthiness.

6. Quicker and Better Business Decisions

In partnership, there are many partners. Every partner has the right to be consulted. Hence business problems can be thoroughly discussed and the best decisions can be arrived. “Two or more persons are better than one”. Partners meet often and take decisions promptly. Thus it avoids taking hasty business decisions.

7. Sharing of Risk

The risk in a business is shared by more persons. The burden of every partner will be much less as compared to the burden of sole trader. Further, the business expansion will not be hampered for fear of risk.

8. Relationship between Reward and Work

The partners work hard to earn more profits. There is a direct relationship between hard work and reward. The more they work, the more will be the reward.

9. Protection of Minority Interests

All important matters connected with the business are decided only by unanimous agreement of all the partners. So the majority of partners cannot disregard the interest of the minority partners. Thus minority interest is well protected.

10. Flexibility

By mutual consent the partners can change the nature of business easily as they like. So business can always be responsive to changing needs. Its price policy, capital, profit sharing ratio etc. can be changed easily.

11. Close Supervision

Wastages can be avoided as the partners themselves look after the business. They have direct access to the employees and can encourage them for more production. The management of partnership is much cheaper as compared to a joint stock company where experts are paid higher salaries.

12. Easy Dissolution

The partnership can be easily dissolved on insolvency, lunacy or death of a partner. If the partnership is at will, then any partner can get the firm dissolved by giving a notice to other partners. No legal formality is required at the time of dissolution.

13. Better Human and Public Relations

Presence of more number of partners help to develop personal touch with the employees, customers, government and the public. Cordial relations with the public help to enhance the goodwill of the firm.

DISADVANTAGES

The following are the disadvantages of partnership

1. Unlimited Liability

Every partner is jointly and severally liable for the entire debts of the firm. A partner has to suffer not only for his mistakes but also for the lapses and dishonesty of other partners. Unlimited liability discourages many people from becoming a partner in the firm.

2. Limited Resources

The resources of partnership firm is limited. The borrowing capacity of the partners is also limited. Therefore, partnership form of business is not suitable for undertaking business involving huge investment of capital.

3. Danger of Implied Agency

The acts of partners legally bind the business and every other partner in the normal course of business. A dishonest or inefficient partner may bring loss to others by his actions. An innocent partner may be required to loose his personal assets for the mistake on the part of other partners.

4. Distrust

The distrust among partners is the main cause for the dissolution of partnership firms. It is difficult to maintain harmony among partners because they may have different opinions and may not agree unanimously on certain matters. Lack of confidence may lead to misunderstanding and quarrels and it will result in dissolution of the firm.

5. Limitation on Transfer of Share

No partner can transfer his share to a third party without the consent of the other partners. If a partner wants to withdraw his share, it is not possible without the consent of other partners. This makes investment in a partnership firm non-liquid, fixed and less attractive.

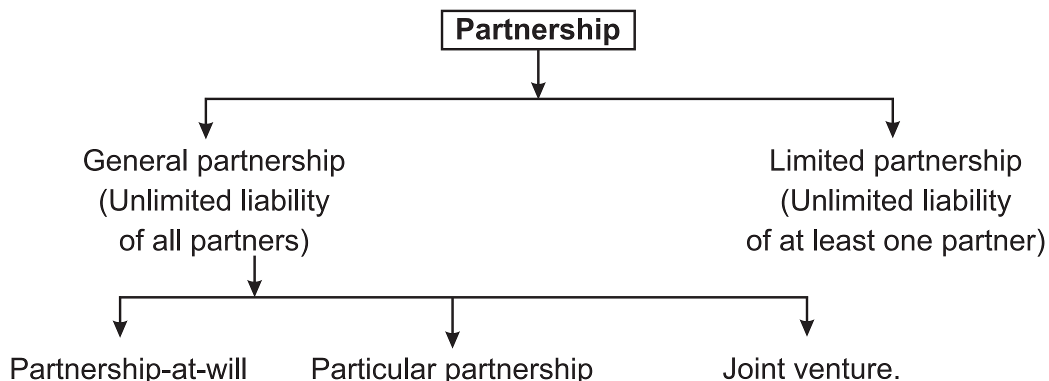
6. Lack of Continuity

Dissolution of partnership

A partnership comes to an end with the retirement, incapacity, insolvency and death of a partner. Even a single partner, if he is dissatisfied with the business, can dissolve the partnership. The lack of trust among partners can also lead to dissolution.

3.5. TYPES OF PARTNERSHIP FIRM

Different kinds of partnership may be explained as follows.



1. General or Unlimited Partnership

A partnership in which the liability of all the partners is unlimited is known as unlimited partnership. All the partners can take part in the working of the business. In India, only this kind of partnership exists. General partnership can be classified into three types such as partnership-at-will, particular partnership and joint venture. They are discussed below.

a. Partnership–at–will

Partnership-at-will is a partnership which is formed to carry on business without specifying any period of time. The life of such a partnership continues as long as the partners are willing to continue it as such. The partnership can be terminated, if any partner notifies his desire to quit.

b. Particular Partnership

It is a partnership established for a stipulated period of time or for the completion of a specified venture. It automatically comes to an end with the expiry of

the stipulated period or on the completion of the specified venture, as the case may be. For example, a partnership may be created for one year only. When the time lapses, the partnership comes to an end.

c. Joint Venture

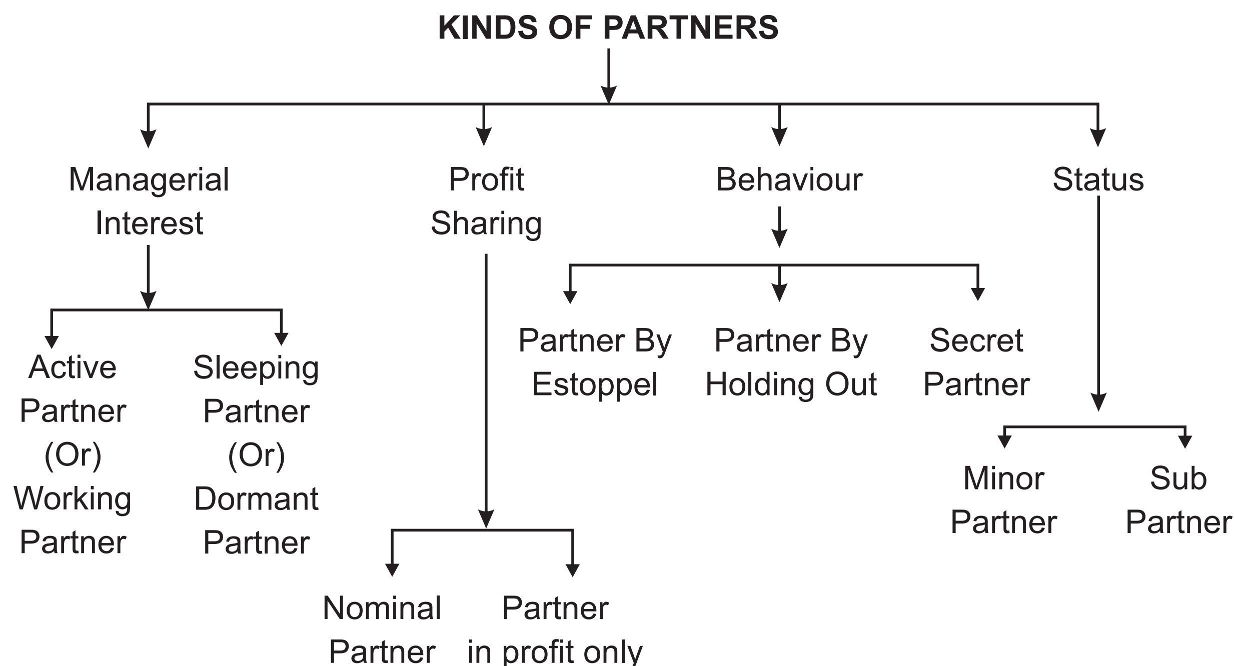
A joint venture is a temporary partnership which is formed to complete a specific venture or job during a specified period of time. Every partner does not have the right of implied agency. No partner can withdraw his interest in the firm before the completion of the venture. For example, a partnership is formed for the construction of a building. The partnership comes to an end if the construction is over.

2. Limited Partnership

A partnership in which the liability of the partner is limited is called limited partnership. The Law does not permit the formation of a limited partnership in India. But in Europe and U.S.A. limited partnership is allowed. A limited partnership firm must have at least one partner whose liability is unlimited. The liability of remaining partners is limited. Thus limited partnership consists of two types of partners, general partner and limited partner.

3.6 KINDS OF PARTNERS

There are different kinds of partners classified on the basis of managerial interests, profit sharing, behaviour and and status. They are as follows.



1. Active Partner

A partner who takes active part in the management of the partnership firm is known as active or working or managing or general partner. His liability is unlimited.

2. Sleeping Partner or Dormant Partner

The partners who merely contribute capital and do not take active interest in the conduct of the business of the firm are called sleeping or dormant or financing partners.

3. Nominal or Ostensible Partner

He is a partner who neither contributes capital nor takes any part in the management of the firm. He lends his name to be used as partner in the business to increase the reputation of the firm. They are not eligible for a share in the profit. They are also liable to the creditors for the debts of the firm.

4. Partners in Profit Only

A person who shares the profit of a firm but does not share the loss, is called "partner in profit only". Usually he has no voice in the management of the firm. But his liability to third parties is unlimited.

5. Partner by Estoppel

A person may not be really a partner in the business. But by his behaviour he makes outsiders believe that he is a partner in the business. Then, he is liable to such outsiders who advance money to the firm or enter into a contract under such false belief. Such a person is known as "partner by estoppel". He cannot later on deny that he is not a partner.

6. Partner by Holding out

When a person who is not really a partner in a business, is described as a partner to others, then he must at once deny it when he comes to know about it. If he keeps quiet, then he is liable to other persons who do business with that partnership believing that he is also a partner. Such a person is called partner by holding out.

7. Sub-Partner

When a person makes an arrangement with a partner to share his profit, he is known as a sub-partner. Such a sub-partner has no rights against the firm, as he is not liable for the debts of the firm.

8. Minor as a Partner

A minor is a person who has not completed 18 years of age, where a guardian is appointed by a court, his age of majority extends to 21 years. Legally, a minor cannot become a partner because he is incapable of entering into a contract. He may, however, be admitted to the benefits of partnership with the consent of all partners.

The position of a minor partner may be studied under the following two heads.

a. Position before attaining majority

a) He has a right to share the property and profits of the firm as may have been agreed upon.

b) He has a right to have access to and inspect and take a copy of the accounts of the firm.

c) His liability is confined only to the extent of his share in the profits and property of the firm. Over and above his capital, he is neither personally liable nor his private properties is liable.

b. Position on attaining majority

On attaining majority the minor partner has to decide within six months by giving notice whether he shall continue in the firm or not. If he decides to continue as partner, he becomes liable to the firm from the date, on which he was admitted as minor partner. If he decides not to continue as partner, he is not liable for the debts of the firm after the date of notice.

3.7. RIGHTS, DUTIES AND LIABILITIES OF PARTNERS

Generally, the rights, duties and liabilities of partners are laid down in the partnership deed. In case the partnership deed does not specify the rights and duties, the provisions of Partnership Act 1932 will apply. The Act lays down the following rights and duties of a partner.

1. Rights of Partners

1) Every partner has a right to take part in the conduct and management of the business.

2) Every partner has a right to express opinion on any matter related to the firm.

3) Every partner has a right to be consulted before taking important decisions.

4) Every partner has a right to inspect and take copy of books of account and records of the firm.

5) Every partner has the right to an equal share in the profits of the firm unless otherwise agreed by the partners.

6) Every partner has the right to receive interest on loans and advances at the rate of 6% per annum.

7) Every partner has the right to be indemnified for the expenses incurred and losses sustained by him in the ordinary conduct of the firm's business.

8) Every partner has an equal right to use the assets of the firm for its business.

9) No new partner can be admitted into partnership without the consent of other partners.

10) Every partner has a right to retire from the firm.

3.7. Duties of Partners

The duties of partners can be classified into

1.Absolute duties and 2.Qualified duties.

1. Absolute Duties

Absolute duties are fixed by law which cannot be violated by partners agreement. These duties are applicable to all partnership.

1. Every partner must act diligently and honestly in the discharge of his duties to the maximum advantage of all partners.
2. Every partner must act in a loyal and faithful manner towards each other.
3. Every partner must act within the scope of the authority entrusted to him.
4. Every partner is bound to share the losses of the firm equally unless otherwise agreed.
5. Every partner must indemnify the firm against loss sustained due to his willful negligence in the ordinary course of business.
6. No partner can transfer or assign his interest in the firm to others without the consent of other partners.
7. Every partner must maintain and render true and correct accounts relating to the firm's business.
8. No partner can engage himself in a business which is likely to compete with the business of the firm.
9. Every partner should use the firm's property only for the firm's business and interest.
10. No partner can make any secret profit by way of commission on purchases or sales effected on behalf of the firm.

2. Qualified Duties

Qualified duties given in the Act can be modified by an agreement of partners entered into.

3. Liabilities of partners.

1. Every partner is liable for the debts of the firm to an unlimited extent, jointly and severally.
2. A retiring partner is liable for all the debts incurred before his retirement

3. An incoming partner is liable only for the debts incurred by the firm after his admission into the partnership.
4. In case of deceased partner, his legal representatives are liable only for the debts incurred by the firm before his death.
5. In the case of minor partner, he is not personally liable for the debts of the firm. Only his share in the profits and assets of the partnership is liable for the debts of the firm.
6. Every partner is liable to make good the loss that the firm or other partners suffer as a result of his negligence.

3.8. PARTNER'S EXPRESS AND IMPLIED AUTHORITY

The authority of a partner means the capacity of a partner to bind the firm by his act. The authority may be express or implied.

1. Partners express authority

Where the authority to a partner is expressly conferred by an agreement, it is called express authority. The firm is liable for all the acts of by such partners done within such authority.

2. Implied Authority of a Partner

An implied authority is a right vested with a partner to be used in emergency situations to protect the interest of the firm. Where there is no partnership agreement or where the agreement is silent, "the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm". [sec.19(1)]. The authority of a partner to bind the firm is called "implied authority".

3. A partner has Implied Authority in the following cases

1) Buying, selling and pledging the goods of the firm.
2) Receiving payment of the debts due to the firm and issuing receipts for them.
3) Settling accounts with the persons dealing with the firm.
4) Engaging servants for the partnership business.
5) Borrowing and repaying loans for the firm.
6) Drawing, accepting, endorsing bills and other negotiable instruments in the name of the firm.
7) Operating the bank account on behalf of the firm.
8) Taking legal action and defending such actions on behalf of the firm.

4. A Partner has no Implied Authority in the following cases

1) To submit a dispute relating to the business of the firm to arbitration.

2) To open a bank account on behalf of the firm in his own name.

3) To compromise or relinquish any claim or portion of a claim by the firm.

4) To withdraw a suit or proceeding on behalf of the firm.

5) To admit any liability in a suit or proceeding against the firm.

6) To acquire immovable property on behalf of the firm.

7) To transfer immovable property belonging to the firm.

8) To enter into partnership on behalf of the firm.

3.9. PARTNERSHIP DEED

A partnership firm can be formed through an agreement among two or more persons. In India this agreement may be oral or in writing. But it is desirable to have it in writing to avoid any misunderstanding among the partners in future. All the terms and conditions of partnership are included in the agreement. The partnership agreement is also known as Partnership Deed or Articles of Partnership.

Contents of Partnership Deed

A partnership deed will usually provide for the following matters.

1. Name of the firm.
2. Date of agreement and principal place of business.
3. Names and addresses of all the partners.
4. Nature of business proposed to be carried on by the firm.
5. Duration of the partnership, if any.
6. Amount of capital contributed by each partner.
7. Amount of withdrawal of each partner.
8. Profit sharing ratio.
9. Salary payable to active partner or partners.
10. Interest on capital and interest on drawings.
11. Procedure for admission or retirement of partners.
12. Manner of dissolving the firm and the mode of settlement of accounts on such dissolution.

13. Maintenance of books of accounts and their audit.
14. Interest to be allowed on partner's loans and advances to the firm.
15. Mode of valuation of goodwill on admission, retirement or death of a partner.
16. Procedure for settlement of disputes among partners by arbitration.

The contents of a partnership deed can be altered only with the consent of all the partners.

3.10 REGISTRATION OF FIRM

Registration of a partnership firm in India is not compulsory. It is only optional. Indian Partnership Act, 1932, provides that if the partners so desire, they may register their firms with the registrar of firms of the state. The procedure for registration is explained below.

1. Procedure for Registration

A partnership firm can be registered at any time by filing a statement in the prescribed form. The form should be duly signed by all the partners. It should be sent to the registrar of firms along with the prescribed fee. The statement should contain the following particulars.

1. Name of the firm
2. Principal place of its business
3. Name and address of each partner
4. Date of admission of each partner
5. Date of commencement of business of the firm
6. Duration of the firm

On receipt of the statement and the fees, the registrar makes an entry in the register of firms. A certificate is issued by the registrar which is known as Certificate of Registration. The firm is considered to be registered when the entry is made. Any change in the above particulars must be communicated to the registrar of firms within a reasonable period of time so that necessary alteration may be made in the register of firms. This register is open for inspection on payment of a nominal fee.

2. Effect of Non-Registration

Registration of partnership is only optional in India. But if a firm is not registered, it has to face the following drawbacks.

1. A partner of an unregistered firm cannot file any case against the firm or against any other partner, including an ex-partner for enforcing his contractual rights under the partnership agreement or under the Act.

2. An un-registered firm cannot file any suit against third parties in any civil court for recovering the money due.
3. Any third party can take legal action against the business or the partners.
4. The firm cannot take legal action against its partners.
5. An unregistered firm cannot enforce its claims against third parties for recovering a sum exceeding rupees one hundred.
6. A partner cannot sue for dissolving the firm or realising the property of the dissolved firm or for the settlement of accounts on dissolution.
7. The firm forfeits its rights in restricting the outsiders from using the trademarks and copyrights of the firm.

3.11. DISSOLUTION OF PARTNERSHIP FIRM

Dissolution of partnership firm means putting an end to the relationship among the partners. This may be of two types: they are

a) Dissolution of firm

b) Dissolution of partnership

a) Dissolution of firm

Dissolution of firm means dissolution of partnership. On dissolution of firm, partnership business comes to an end. Its assets are realised and the creditors are paid off. The business cannot be continued after dissolution of partnership firm. For example A, B and C are partners in a business. If all the three partners decide to dissolve, it is known as “dissolution of the firm”.

b) Dissolution of partnership

Dissolution of partnership means the termination of the original partnership agreement. A partnership is dissolved by insolvency, retirement, expiry or completion of the term of partnership. The business will continue after dissolution of partnership. For example: A, B and C are partners in a business. If ‘A’ retires, ‘B’ and ‘C’ can continue the business which is known as dissolution of partnership.

The various circumstances leading to dissolution of partnership firm can be summarised by taking the first letters used in the term “Dissolution”.

D - Death of partner

I - Incapacity of a partner

S - Stipulated period of partnership completed in the case of particular partnership

S - Serious misconduct of a partner

O - Object is completed (Particular partnership)

L - Lunacy of a partner

U - Unavoidable continuous loss

T - Transfer of interest of the firm

I - Insolvency of a partner

O - Objectionable unlawful objectives

N - Notice of dissolution by a partner.

Differences Between Dissolution of Partnership and Dissolution of Firm

The following are the main differences between dissolution of partnership and dissolution of firm.

1. In the case of dissolution of partnership, only one or more of the partners terminate their connections with the firm whereas all the partners terminate their connections with the firms in the case of dissolution of firm.

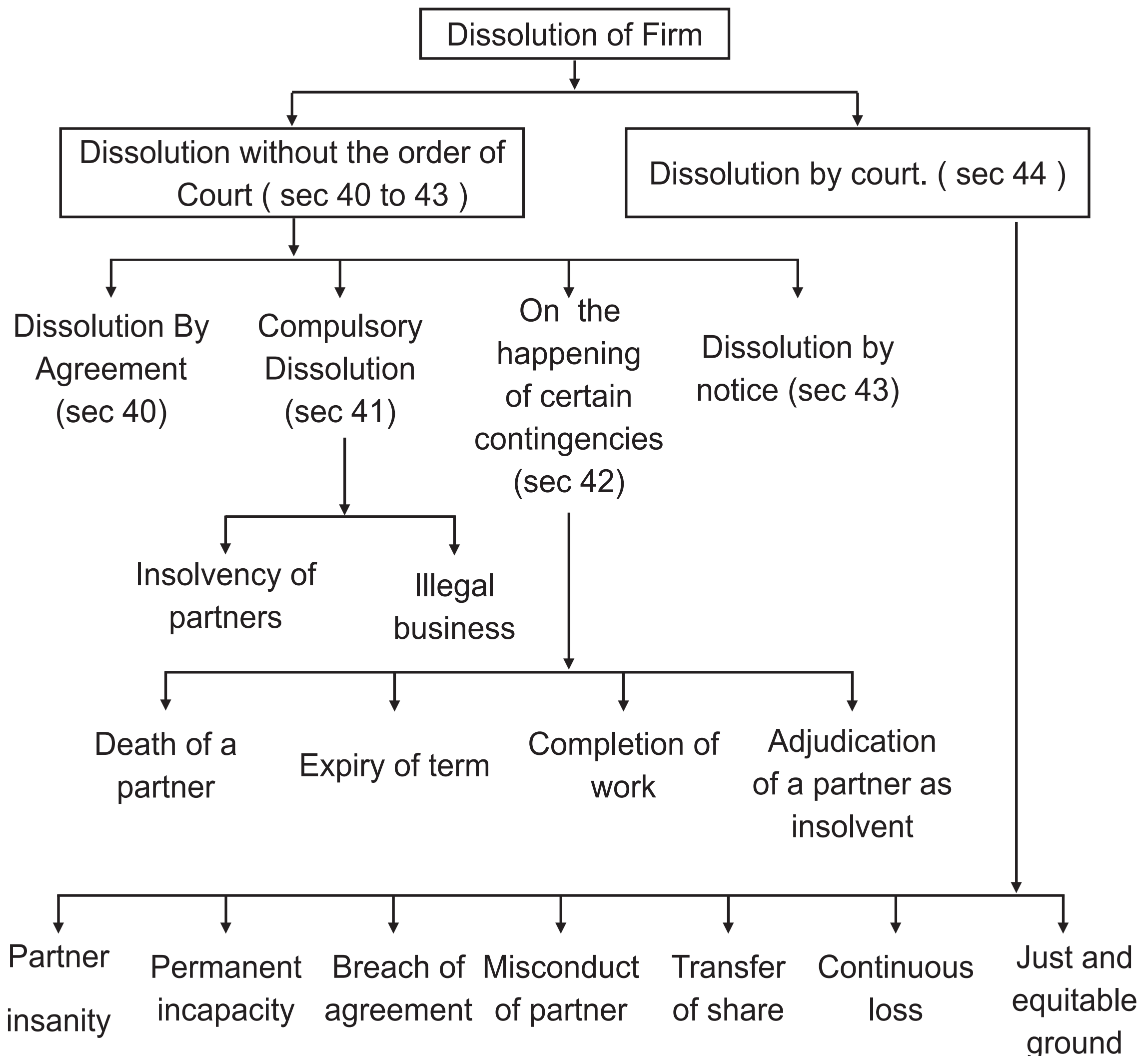
2. Dissolution of partnership may or may not bring the business of the firm to an end, but dissolution of the firm brings the business of the firm to an end.

3. In dissolution of partnership, the business will continue even after dissolution But business cannot be continued in the case of dissolution of firm.

4. Dissolution of partnership need not necessarily results in the dissolution of firm, whereas dissolution of firm necessarily results in dissolution of partnership.

Modes of dissolution of firms

The Partnership firm may be dissolved in any one of the following ways.



1. Dissolution by Agreement (Sec.40)

A partnership is created and dissolved by an agreement. A firm may be dissolved by an agreement either with the consent of all partners or in accordance with the contract among the partners.

2. Compulsory dissolution (Sec 41)

A firm is compulsorily dissolved either by the agreement of all the partners or on the insolvency of all the partners except one. It may also be dissolved on the happening of an event which makes the object of the firm unlawful. Example, the passing of Prohibition Act, declaration of war with another country.

3. Dissolution on the happening of certain contingencies (Sec 42)

A partnership may be dissolved on the happening of the following contingencies

a) Death of a partner.

b) Expiry of the time, if partnership is for a fixed period.

c) Completion of the venture for which the firm was formed.

d) Adjudication of a partner as an insolvent.

4. Dissolution by notice of partnership-at-will (Sec 43)

Where the partnership is at will, the firm may be dissolved by any partner by giving a notice in writing to all the other partners of his intention to dissolve the firm.

5. Dissolution through Court (Sec.44)

Any partner may bring a suit in a court of law to get the partnership dissolved on any of the following grounds.

(i) Partner's Insanity

If any partner becomes insane, the court may order dissolution.

(ii) Permanent Incapacity

When a partner becomes permanently incapable of doing business the court may order dissolution.

(iii) Persistent Breach of Agreement

If a partner persistently violates the agreement and the other partner finds it impossible to do business in partnership with him, then the other partner can move for dissolution.

(iv) Misconduct of a Partner

If any partner is guilty of misconduct (misuse of money) then any partner can file a suit for dissolution of the firm.

(v) Transfer of Share

When a partner transfers his share in the business to a third party without the consent of other partners, then the other partners can move the court for dissolution.

(vi) Continuous Loss

When the business of the firm cannot be carried on except at a loss, the court order for dissolution.

(vii) Just and equitable grounds

When the court feels that it is just and equitable, it may order for dissolution of the firm. E.g., if A and B are partners but do not speak to each other, the court may order for dissolution.

Points to Remember

❖ Meaning, Definition and Nature

The partnership is the result of:

a. Need for more capital in the business

b. Need for more managerial ability

c. Need for diffusion of risk

d. Need for greater amount of specialisation

❖ Features

1. Agreement 2. Multiplicity of person 3. Contractual relation 4. Lawful business. 5. Sharing of profits 6. Agency relationship. 7.Unlimited liability 8. Joint and several liability 9. No separate legal entity 10. Implied agency 11. Utmost good faith 12. Non-transferability of interest. 13. Registration.

❖ Differences between partnership and sole trader.

1.Specific Act 2.Number of members. 3.Agreement. 4.Registration. 5.Ownership and control. 6.Management. 7.Capital. 8.Liability. 9.Implied agency. 10.Division of profit or loss. 11.Decision-making. 12.Division of work. 13.Secrecy. 14.Economic strength. 15.Survival.

❖ Advantages

1.Ease of formation. 2.Registration not compulsory. 3.Larger financial resources. 4.Greater managerial talent. 5.More credit standing. 6.Quicker and better business decisions. 7.Sharing of risk. 8.Relationship between reward and work. 9.Protection of minority interests. 10.Flexibility. 11.Close supervision. 12.Easy dissolution. 13.Better human and public relations.

❖ Disadvantages

1.Unlimited liability. 2.Limited resources. 3.Danger of implied agency. 4.Distrust. 5.Limitation on transfer of share. 6.Lack of continuity.

❖ Type of partnership firms.

1.General or unlimited partnership. 2.Partnership-at-will. 3.Particular partnership. 4.Joint venture. 5.Limited partnership.

❖ **Types of partner**

1. Active partners 2. Sleeping partners 3. Nominal partners 4. Partner-in-profit only 5. Partner by estoppel 6. Partner by holding out. 7. Secret partner 8. Sub-partner. 9. Minor as partner.

❖ **Rights of partners**

1. Right to take part in the conduct and management of the business.2. Right to expression opinion. 3. Right to be consulted. 4. Right to inspect and take copy of books of accounts and records of the firm. 5. Right to an equal share in the profits 6. Rights to receive interest on loans and advances. 7. Right to indemnified for the expenses incurred. 8. Right to use the assets of the firm for its business. 9. No new partner can be admitted without the consent of other partners. 10. Right to retire from the firm.

❖ **Duties of partners.**

1. Act diligently and honestly in the discharge of his duties. 2. Act in a loyal and faithful manner towards each other. 3. Act within scope of the authority entrusted to him. 4. To share the losses. 5. Every partner must indemnify the firm against loss sustained due to his wilful negligence. 6. No partner can transfer his interest. 7. Every partner must maintain and render true and correct accounts of the firm. 8. No partner can engage himself in a business which is likely to complete with the firm. 9. Every partner should use the firm's property only for the firm's business and interest.
10.No partner can make any secret profit.

❖ **Liabilities of partners.**

1.Unlimited liability for the debts of the firm 2. Should make good the loss caused by his act 3. A retiring partner is liable for all the debts 4. An incoming partner is liable for all debts after his admission 5. The legal representative of a deceased partner is liable to pay for the debts 6. Minor partner shares profit only.

❖ **Partners express authority**

Where the authority to a partner is expressly conferred by an agreement, it is called express authority.

❖ **Implied authority of a Partner**

An implied authority is a right vested with a partner to be used in emergency situations to protect the interest of the firm.

❖ **Partnership deed and its contents.**

Partnership is the result of an agreement between the partners, which is known as partnership deed.It must be in writing.

❖ **Contents**

1. Name of the firm and names of all the partners 2. Nature of the Business. 3.Duration of the Business 4. Profit sharing ratio 5. Capital contributed by partners 6. Salary, commission to any partner 7. Interest on partners' capital and drawings 8. Rights, duties and obligations of all partners 9. Any other matter.

❖ **Dissolution of a firm.**

Dissolution of partnership firm means putting an end to the relationship among the partners.

❖ **Methods of dissolution.**

1. Dissolution by consent 2. Compulsory dissolution 3. Contingent dissolution 4.Dissolution by notice 5. Dissolution by court order.

❖ **Circumstances leading to dissolution.**

1. Death of a partner 2. Incapacity of a partner 3. Serious misconduct of a partner 4. Stipulated period is over 5. Object of the business completed 6. Lunacy of a partner 7. Un-avoidable continuous loss 8. Transfer of interest by a partner 9. Insolvency of a partner 10.Unlawful business 11. Notice by a partner.

QUESTIONS

A. Objective Type

I. Multiple Choice

1. A partnership is formed by

   a) Agreement

   b) Relationship among persons

   c) The direction of government

2. The basis of partnership is

   a) Utmost good faith

   b) Money available for investment

   c) Desire to work together

3. A partnership firm may be registered under

   a) 1949 Act

   b) 1956 Act

   c) 1932 Act

4. Registration of partnership is

   a) compulsory

   b) optional

   c) not necessary

5. In partnership there exists a relationship of

   a) principal and agent

   b) owner and servant

   c) employer and employee.

Ans: 1 (a) ; 2 (a) ; 3 (c) ; 4 (b) ; 5 (a).

II. Fill in the blanks

1. The profit and loss of a partnership firm is shared in the _____ among the partners.
2. The partners liability in India is _____
3. The maximum number of members in non-banking firm is _____
4. A partner who does not take part in the working of the firm is called _____ partner.

Ans: 1. Agreed ratio, 2. Unlimited, 3. 20, 4. Sleeping.

III. Short Questions

1. Define Partnership
2. What are the minimum and maximum number of members in the partnership firm?
3. What is the relationship that exits among partners?
4. Who is a dormant partner?
5. What is limited partnership?
6. What is a partnership deed?
7. Define implied authority of a partner
8. What is joint and several liability?
9. Who is a minor? Can a minor become a partner?
10. Bring out the difference between dissolution of partnership and dissolution of partnership firm.

IV. Paragraph Questions

1. Explain the position of minor in the partnership firm.
2. Explain the procedure for registration of a partnership firm.
3. What are the drawbacks of non-registration of partnership firm?
4. What are the contents of partnership deed?
5. Describe the various kinds of partners.

V. Essay type Questions

1. Explain the basic features of partnership
2. What are the advantages and disadvantages of partnership firm?
3. Explain the rights and duties of partners
4. What are the circumstances under which a partnership firm is dissolved?
5. Compare and contrast a partnership with a sole proprietorship.

CHAPTER - 4
JOINT STOCK COMPANIES – I

"A Company is a long Shadow of the Boss".

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 4.1. Meaning – Definition – Features – Merits – Demerits.
- ❖ 4.2. Differences between Partnership firm and Joint Stock Companies.
- ❖ 4.3. Kinds of Companies.
- ❖ 4.4. Privileges of a Private Limited Company.
- ❖ 4.5. Differences between Private Limited Company and Public Limited Company.
- ❖ 4.6. Formation of a Company.
- ❖ 4.7. Basic Documents – Memorandum of Association – Meaning – contents.
- ❖ 4.8. Articles of Association – Meaning - Contents.
- ❖ 4.9. Prospectus – Definition – Contents.
- ❖ 4.10. Shares – Meaning – Kinds.
- ❖ 4.11. Allotment of Share – Meaning – Definition – Share Certificate –Calls. – Forfeitures – Issue of shares – at par- at premium – at discount.
- ❖ 4.12. Debenture - Meaning – Kinds.
- ❖ 4.13. Differences between shares and debentures.

4.1. JOINT STOCK COMPANY

With the advent of Industrial Revolution and the factory system of production, large scale production has become the order of the day. To meet the ever-expanding needs of the fast growing population, large-sized industrial organisation has become

indispensable. The traditional forms of business units, namely, sole proprietary concerns and partnership firms, with their limited financial resources and managerial capability, cannot meet the challenges forced by the need for massive production and speedy distribution. Joint stock company form of organisation provides the key to this problem. This is better suited for mobilising large capital resources and ensuring highly sophisticated managerial skills for running giant-sized industrial enterprises.

4.1. Company – Meaning

The term "company" refers to a body corporate. In other words, it is a body incorporated in accordance with the provisions of a specified Act. It is viewed to be a person created by law – a jurisidical person. Its legal entity is distinct from its members and independent of even its promoters who give birth to it.

4.1. Definition

In the words of Lord Justice Lindley, " By a company we mean, "an association of many persons who contribute money or money's worth to a common stock and employ it in some trade or business and also share the profit and loss, as the case may be, arising therefrom".

Even this definition is incomplete; it is Haney's definition, which brings out all its essentials. He observes, " A company is an incorporated association; it is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal."

4.1. Salient Features

1. Separate legal entity

A company is a person created by law. It means that it comes into existence only by complying with all formalities prescribed under the Companies Act, 1956. It enjoys a separate personality of its own, different from the members composing it. This enables a company to enter into valid contracts with others including its members and deal with the property in any way it likes. It can sue others in its own name and be sued in its own name by others including its members.

2. Perpetual Succession- Continuity of Life

"Members may come and go but the company can go on forever" (Lord Gower). This is because company's existence does not depend upon the existence of even promoters who were instrumental in its formation. Neither change in the membership of the company nor the death of its members has any impact on the continuity of its life.

3. Common Seal

Though the separate personality of the company is legally recognised, it needs human agency to act. Obviously it cannot sign. Any contract entered into by a company, to be valid, must bear the official seal of the company.

4. Limited Liability

The liability of the members of a company is generally limited to the value of shares. When once the full value of the shares is paid up, there is no more liability for the shareholders. The feature of limited liability attracts a large number of investors to subscribe to the shares of the company.

5. Easy Transferability of Shares

In the case of public limited companies, their fully paid shares can be transferred to others without any difficulty. However, in the case of private limited companies, the right to transfer the shares is subject to certain restrictions.

4.1.1. Merits of the Company form of Organisation

The distinctive features of a joint stock company are in fact its merits. They make this form of organisation very popular and better fitted for starting large-sized business ventures.

1. Stability (Perpetual Life)

While certain contingencies such as death, insanity or insolvency of partners lead to the dissolution of partnership, they do not have any effect on the continued existence of a company. The company enjoys perpetual succession despite change in its membership or change in its Board of directors. Large sized enterprises which take a long time to reach profit earning stage can be started only as company form of organisations which ensures long life.

2. Limited Liability

The liability of a member of a joint stock company is limited to the amount remaing unpaid on his shares. Once the full value of the shares is paid, a shareholder will not be called upon to contribute anything further even if the assets are inadequate to meet business debts. In view of this feature of limited liability, people come forward readily to invest in the shares of joint stock companies. Thus the savings of the community which lie scattered can be easily mobilised for financing business enterprises.

3. Easy and Speedy Transferability of Shares

The fully paid up shares of a public limited company can be easily transferred from one person to another by following the procedure prescribed by the Companies Act, 1956. This facility is another attraction for the investing public to subscribe to the shares of the company.

4. Professionalisation of Management

In a company form of organisation there is complete divorce between ownership and management. Though shareholders are the real owners, they do not have any right to manage its affairs. Management of a company is entrusted to a Board of Directors elected by the shareholders from among themselves. The Board can secure the services of experts in various fields of production and management.

5. Economies of large scale

In view of the suitability of the company form of organisation for undertaking large sized industries, it can reap all the advantages of economies of large scale operation. Further there is scope for tremendous growth through expansion of its activities as raising of capital is not a problem for sound companies.

6. Better credit

A company enjoys greater public confidence and reputation in the capital market as its functioning is subject to many legal restrictions with a view to protecting the interest of all the shareholders.

In view of these merits joint stock form of organisation is very popular and is preferred to other forms especially for setting up large sized industrial undertakings.

4.1.2. Demerits of the Company form of Organisation:

1. Complicated legal formalities

The legal formalities to be complied with at the time of forming a company are complicated and difficult. Even after incorporation, its functioning is subject to severe restrictions. A number of documents have to be filed with the Registrar of joint stock companies from time to time and every failure in this regard invites penalties.

2. Heavy cost of Floating a company

At the promotion and incorporation stage itself, the company has to get the services of specialised professionals. Many documents are to be drafted and printed. Further, huge expenditure is to be incurred for publicising the issue of prospectus, inviting the public to subscribe to the shares of the company. Cost of merchant bankers to whom the entire issue of shares is entrusted, also adds considerably to the cost of raising capital.

3. Separation of Ownership and Control

Though divorce of ownership and control is an advantageous feature of a company form of organisation, it also acts as a setback in that the shareholders are not entitled to participate directly in its management. Their interest may not be well taken furthering their own selfish motives, and thereby harming the larger interest of the company and the shareholders.

4. Fraudulent Promoters

Unscrupulous promoters may mobilise large capital through attractively designed prospectus, swindle the money and disappear, despite the stringent legal restrictions. Shareholders lose their entire money. Such companies, known as 'fly by night companies' are a threat to a healthy capital market.

5. Oligarchic Management

In theory, the management of a company is democratic, as it is in the hands of the Board of Directors who are elected by the shareholders from among themselves. However, in reality it proves to be a case of oligarchy. Due to the apathy and ignorance of a vast number of shareholders and because of their being widely scattered throughout the length and breadth of the country, a very few shareholders tend to get themselves elected as directors and manage the affairs of a company. Since the voting strength depends on the number of shares, the power is concentrated in a few hands. Also the shareholders attending the meeting is far less. They do not have any voice in the management and the general meetings prove to be only a farce.

4.2 Differences between a partnership firm and joint stock company

S.No	Basis of Difference	Partnership Firm	Joint Stock Company
1.	The Acts	Partnership firm is governed by the Indian Partnership Act, 1932	Companies are governed mainly by the provisions of the Companies Act, 1956
2.	Registration	Registration with the Registrar of Firms is only optional.	Registration with the Registrar of Companies is compulsory.
3.	Number of members	A minimum of two persons is necessary to form a partnership. The maximum number is restricted to 10 in the case of banking business and to 20 in other types of businesses.	The minimum number of persons required for starting a private limited company is 2. while it is 7 in the case of a public limited company. The maximum number of members is restricted to 50 exclusive of present or past employee - members in the case of a private limited company and it is limitless for a public limited company.

(1)	(2)	(3)	(4)
4.	Legal status	Partnership firm has no separate existence. Partners collectively constitute the firm.	It is an artificial person created by law. Its existence is independent of its members.
5.	Liability	The liability of a partner is joint, several and unlimited. Personal assets of the individual partners can also be attached for satisfying the firm's debts. Any one partner can also be sued for this purpose.	The liability of the shareholder is limited to the unpaid amount of shares held. If the shares are fully paid up, no further liability is attached to the shareholders, however rich they may be.
6.	Transfer of Shares	A partner cannot transfer his interest in the firm without the consent of all other partners	In a public limited company, shares are fully transferable However, certain restrictions are placed on transfer of shares in the case of private limited companies.
7.	Management	Management of a firm is carried on by all or by any of them acting for all. In other words, every partner is entitled to participate in the management.	Direct participation of shareholders in the management of the company is not allowed. It is entrusted to the Board of Directors elected by the members
8.	Stability	A partnership firm is not stable. Its continuity is threatened by certain contingencies such as death, insanity or insolvency of any one or all its partners	A company is stable as it is totally unaffected by any such contingencies.
9.	Procedural complexities	Both for formation and dissolution, the procedures are simple.	Both the formation and winding up are subject to many legal formalities.

(1)	(2)	(3)	(4)
10.	Financial resources	The capital contribution as well as the finance that can be raised tend to be limited.	The scope for mobilising larger resources is very wide.
11.	Membership	In a partnership only individuals can become its members.	In a company, an institution can also become a member by purchasing its shares.
12.	Nature	Partnership is the relation between persons who have agreed to share the profits or losses of a business.	A company is an artificial person.
13.	Mutual relationship of the members	In the partnership, each partner is an of agent of the others.	The members of the company are not its agents or representatives.
14.	Audit	Audit of accounts is not except . uncertain circumstance.	It is essential for every company to get its accounts annually audited by chartered accountant
15.	Dissolution	Partnership can be mutually dissolved at time.	Legal formalities for winding up are many.

4.3 Kinds of Companies

Joint Stock Companies can be classified on the basis of incorporation, nature of liability, extent of public interest, ownership, nationality etc. Let us examine briefly the different kinds of companies.

1. On the basis of Incorporation

Any company is to be incorporated under an Act. The provisions of the particular Act under which it is established governs its working. Companies of this kind are of three types. They are:

a. Chartered Companies

Companies established as a result of a charter granted by the King or Queen of a country are known as chartered companies. The charter issued, governs their functioning.

Examples: East India Company and Bank of England. The provisions of the Companies Act are not applicable to them. In India, such companies do not exist now.

b. Statutory Companies

Companies established by Special Acts of Parliament or State Legislatures are called statutory companies. The special Acts under which they are established regulate their functioning. Reserve Bank of India, Life Insurance Corporation of India etc. are of this type.

c. Registered Companies

Companies which are registered under The Companies Act, 1956 are called registered companies. A vast majority of companies we come across belong to this category. Tata Motors Limited, Satyam Computer Services Ltd, EID Parry Ltd, etc belong to this category.

2. On the Basis of Liabilities

On the basis of the extent of liabilities of the shareholders such companies are divided into three categories.

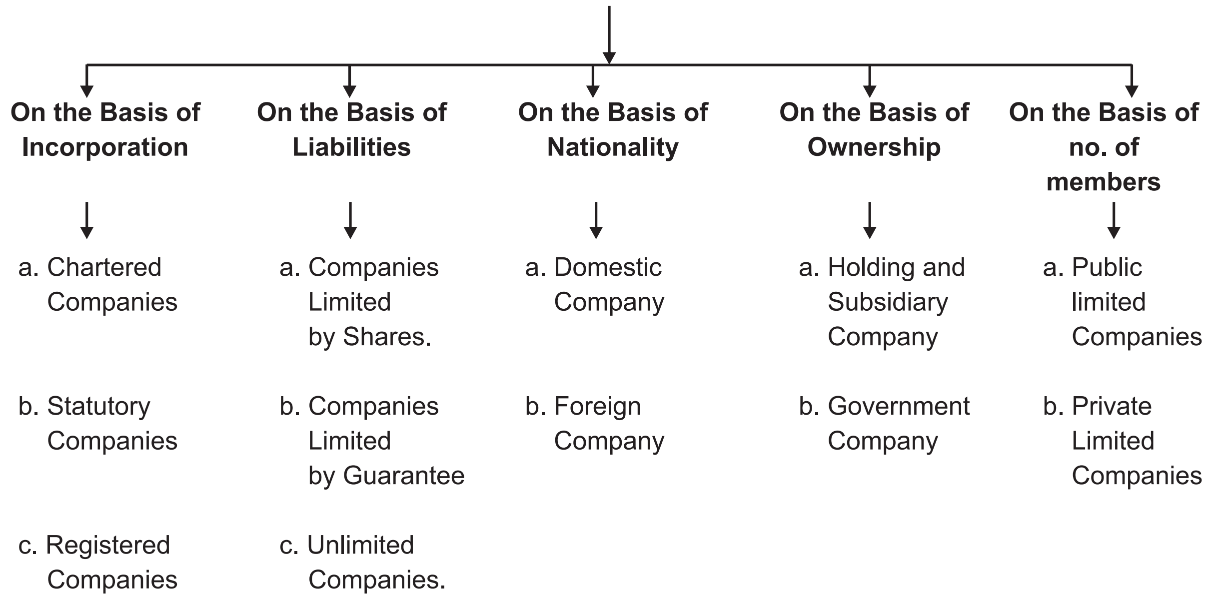
a. Companies Limited by Shares

Here the maximum liability of a shareholder is limited to the amount unpaid on the shares held. Once he pays the full value of shares, he has no further liability. A vast majority of companies in India are of this type.

b. Companies Limited by Guarantee

In a company limited by guarantee the liability of a shareholder is limited to the amount he has voluntarily undertaken to contribute to meet any deficiency at the time of its winding up.

Such a company may or may not have a share capital. If it has a share capital a member's liability is limited to the amount remaining unpaid on his shares plus the amount guaranteed by him. This type of company is started with the object of promoting science, arts, sports, charity, etc. It is clear that its objective is not profit earning. It gets subscription from its members and donations and endowments from philanthropists.



c. Unlimited Companies

The liability of the members of unlimited companies is unlimited. In other words, their liability extends to their private properties also in the event of winding up. Unlimited companies are almost non-existent.

3. Companies on the Basis of Nationality

They are of two types viz domestic companies and foreign companies.

a) Domestic Company

Companies registered under the Companies Act, 1956 or under earlier Acts are considered domestic companies.

b) Foreign Company

Foreign company means a company incorporated outside India but having a place of business in India. It has to furnish to the authorities the full address of the registered or principal office of the company or a list of its directors or names and addresses of the residents in India authorised to receive notices, documents, etc.

4. On the Basis of Ownership

They are of three types viz holding company, subsidiary company and Government Company

a. Holding and Subsidiary Companies

A company becomes a holding company of another

i) if it can appoint or remove all or majority of the directors of the latter company or

ii) if it holds more than 50% of the equity share capital of the latter or

iii) if it can exercise more than 50% of the total voting power of the latter.

The other company which is so controlled is called subsidiary company.

b. Government Companies

A Government company is one in which not less than 51% of the paid up capital is held by the Central Government or by any one or more State Governments or partly by the Central Governments and partly by one or more State Governments. Examples: Bharat Heavy Electricals Limited, Steel Authority of India Limited, etc

A subsidiary of a Government company is also treated as a Government company. A Government company also enjoys a separate corporate existence. It should not be identified with the Government and its employees are not Government employees.

5. On the basis of number of members

a. Public Limited Companies

The public is invited to subscribe to the shares of the company usually by issuing a prospectus. Shares are easily transferable. Minimum number of person is seven and there is no limit to the maximum number of shareholders. The name must end with the word 'limited'.

b. Private Limited Companies

A private limited company is a company which has a minimum paid up capital of rupees one lakh or such higher paid up capital, as may be prescribed. The Articles of Association may prescribe the following.

i. Restricts the right to transfer the shares, if any.

ii. limits the number of its members to 50 not including its present or past employee- members

iii. prohibits any invitation to the public to subscribe to any shares in or debentures of the company.

The name of the company must end with the words " Private Limited".

4.4 Privileges and Exemptions available to a Private Limited Company

A private limited company enjoys several privileges and exemptions. It is therefore said to be an extension of partnership but with the benefit of limited liability. Let us now see some important privileges available to all private limited companies.

i. A private limited company can be incorporated with just two persons. This facilitates easy formation as well as efficient functioning.

ii. A private Limited company can commence business on getting the certificate of incorporation. There is no necessity for getting a certificate to commence business.

iii. A private limited company is prohibited from issuing prospectus for collecting its share capital.

iv. It can proceed to allot shares without having to wait for getting minimum subscription.

v. It is exempted from holding a statutory meeting.

vi. In the case of a public limited company, when further shares are issued, they must first be offered to the existing shareholders. But a private company is exempted from this restriction.

vii. A private company can work with just two directors.

viii. Directors of a private company are not required to file with the Registrar a written consent to act as a director.

ix. Further they need not give any undertaking to take up any qualification shares

Additional privileges enjoyed by independent private limited companies

The term 'independent private limited companies' refers to those which are not subsidiaries of public limited companies.

i. All its directors can be appointed by a single resolution.

ii. Directors need not retire by rotation.

iii A person can be a director of any number of independent private limited companies.

iv. Restriction regarding overall managerial remuneration which is applicable to a public limited company is not applicable to a private limited company.

v. A private limited company is exempted from maintaining an index of its members with their names and addresses.

4.5 Differences between a Private Limited Company and a Public Limited Company

S.No	Basis of Differences	Private Limited Companies	Public Limited Companies
1.	Number of Members	In the case of a private limited company, the minimum number of members is two while the maximum is not to exceed 50 (excluding its employee members whether past or present)	As for the public limited company while the minimum number of members is 7, the maximum is unlimited
2.	Name	The words " Private Limited" must be added at the end of the name of the private limited company	The name of a public limited company must end with the word "Limited "
3.	Articles of Association	A private limited company has to file the Articles of Association of its own with the Registrar of companies	A Public limited company can have either its own Articles or can adopt model set of articles as provided in Table A of the companies Act.
4.	Minimum Subscription	The question of minimum subscription does not arise in the case of a private limited company	A public limited company has to collect minimum subscription as specified in the prospectus, i.e.minimum of 90 % of the Shares issued by the company
5.	Allotment of Shares	Conditions to be satisfied before allotment of shares do not apply to a private limited company	In the case of public limited companies only after collecting minimum subscription and after alloting shares to existing shareholders, allotment to new applicants can begin

(1)	(2)	(3)	(4)
6.	Directors	A private limited company must have at least two directors. They need not retire by rotation. One can act as a director in any number of private limited compaines	In the case of a public limited company, it should have at least three directors. They are subject to retirement by rotation. A person can act as a director for a maximum of 15 companies
7.	Statutory Meeting	A Private limited company need not hold any statutory meeting	A public limited company should hold it within six months from the date of the commencement of business.
8.	Qualification Shares	The directors of a private limited company need not acquire qualification shares so as to be eligible for election as directors	In the case of public limited compaines, the directors should acquire the prescribed qualification shares
9.	Quorum	The minimum number of members to be present in a meeting so as to constitute a valid meeting is two in a private company	Whereas it is five in a public limited company
10.	Managerial Remuneration	In a private limited company, no limit has been placed on managerial remuneration	In a public limited company, the overall managerial remuneration shall not exceed 11 % of the net profits. However, if there is no profit in any year, or if the profits are inadequate, such remuneration shall not exceed the limits prescribed in the act.

(1)	(2)	(3)	(4)
11.	Written consent	A Private limited company need not documents such as list of persons who have given their consent to become the first director of the company	A public limited company has to file the written consent of the directors with the Registrar of companies.
12.	Commencem- -ent of Business	A private company can start its business as soon as it gets the certificate of incorporation	A public company cannot start its business until it has received the certificate of commencement of business
13.	Issue of Prospectus	A private company is prohibited from issuing propectus	A public limited company can issue prospectus.
14.	Transfer of shares	There is restriction on the transfer of shares in this company	Shares of public company are freely transferable
15.	Issue of subsequent shares	Rights issue does not arise	Public company's new shares are offered first to the existing shareholders
16.	Issue of share warrants	A private company cannot issue share warrant	It can issue share warrants
17.	Retirement of directors	In a private company a director is not required to retire at the age of sixty five years.	Public company directors have to retire at the age of sixty five years.

4.6 Promotion and Formation

The term, 'promotion' refers to the process by which the idea of forming a company takes a definite shape resulting in its incorporation. It is in fact the first stage of the formation of a company.

Promoter

It is the promoter who gets the idea of starting a company and undertakes all the preliminary work necessary for its formation.

Palmer explains the significance of the term promoter in the following words. “ A promoter starts a scheme of forming a company, gets together the Board of Directors, retains bankers and solicitors, prepares or gets prepared memorandum and articles of association, provides the preliminary expenses, drafts the prospectus; in a word undertakes to form a company with reference to a given project and takes the necessary steps to get it going”.

Different stages of promotion

The first step consists in successfully choosing one among the many business opportunities, which is likely to be most profitable. Next step consists in examining the feasibility of the project. The amount that may be required for acquiring plant and machinery, building and other fixed assets, working capital requirements are all calculated. He also assesses the availability of raw materials, skilled as well as unskilled labour, power supply, etc, marketability of the product, etc. In other words he examines the viability and profitability of the project. The next stage consists in selecting people who are desirous of associating themselves with his scheme. The amount of capital, the place of its registered office are all settled at this stage. The final stage is the registration.

Incorporation

For registering the company with the Registrar of Companies, the promoter has to initiate a number of steps as outlined below.

1. Approval for the proposed name

A company can choose any name but it should not closely resemble the name of an existing company. Hence the promoter has to get the approval from the Registrar for the proposed name of the company.

2. Filing of Documents

The promoter has to get prepared the following documents and file them with the Registrar of Companies of the State in which the registered office of the company is situated.

i) Memorandum of Association

This document which is of fundamental importance defines the scope of activities of the company. It should contain the name, the place where the registered office is situated, authorised capital and the objects of the business. It should be printed and duly stamped, signed and witnessed. A minimum of two persons in the case of a private limited company and seven in the case of a public limited company must sign the document.

ii) Articles of Association

This contains the regulations connected with the internal management of the company. This document must also be duly stamped and signed by the signatories to the memorandum and witnessed.

iii) Original letter of approval

Original letter of approval of name be obtained from the Registrar and be filed.

iv) A List of Directors

A list of directors who have consented to be its directors must be filed.

v) Written consent to act as directors

The directors have to give their consent in writing to act as its directors. They should also undertake to take the necessary qualification shares and pay for them.

vi) Notice of the Address of the Registered office

vii) Statutory declaration

A declaration stating that all the requirements of law relating to registration have been complied with is to be filed. This declaration must be given by an Advocate of the Supreme Court or High Court, or by a Chartered Accountant who is engaged in the formation of the company or by a person named in the Articles as a director or secretary of the company.

viii) The Registrar will scrutinise all the documents and if he finds them in order, he will issue the Certificate of Incorporation.

This certificate is a conclusive evidence of the fact that the company has been duly registered. A private Limited company can commence business on getting the certificate of incorporation, but a public limited company has to take some more steps for getting another certificate known as certificate for commencement of business.

Issue of Prospectus

The Board of directors should arrange for drafting a prospectus when it wants to approach the public for securing capital. A prospectus contains all essential points which would induce the investing public to apply for shares in the company. A copy of the prospectus must be delivered to the Registrar before issuing to the public.

Minimum Subscription

A company can proceed to allot shares only if minimum subscription specified in the prospectus has been collected in cash.

Statement in Lieu of Prospectus

Where the promoters raise the entire capital through private arrangement, there is no need to issue a prospectus. However, a statement in lieu of prospectus, the contents of which are similar to a prospectus, must be prepared and filed with the Registrar at least three days before allotment.

Filing of further documents

The following documents are also to be filed with the Registrar.

i). A declaration that the minimum subscription stated in the prospectus has been collected in cash.

ii). A declaration stating that each director has paid in cash for the application and allotment on the shares taken up by them.

iii). A declaration that no money has become refundable to applicants because of its failure to obtain permission for shares or debentures to be dealt in on any recognised stock exchange.

iv). A statutory declaration by the Secretary or one of its directors stating that the above requirements have been complied with.

If the Registrar is satisfied that these documents are in order, he will issue a certificate entitling the company to commence business. It is only on getting this certificate, a public limited company can start its business.

Basic documents used in the Company

4.7 Memorandum of Association

It contains " the fundamental conditions upon which alone the company is allowed to be incorporated. It defines the activities the company is permitted to undertake. Any act done which is outside the scope outlined in its memorandum is ultra vires (beyond the powers of) the company and is not binding on it.

4.7.1. Contents of the Memorandum

A memorandum of Association must contain the following clauses viz

1. Name Clause

In this clause the name of a company is mentioned to establish its identity. It is the symbol of its existence. Undesirable name to be avoided. It should not imitate another company's name. If it is a public limited company, it should end with the word 'limited'. If it is a private limited company, it should end with the word 'private limited'.

2. Situation Clause

The State in which a company has its registered office is to be stated here. Exact address within the State need not be given in this clause. It determines the jurisdiction of the Registrar of Companies and of the court.

3. Objects Clause

This is the most important clause as it states the activities of the company. The objects lay down the maximum permitted range of activities. A company has the power to carry on only those types of business which are included in this clause. Any action beyond the powers of the company has no legal effect.

4. Liability Clause

This clause states that the liability of members is limited. In the case of a company limited by guarantee, the amount each member undertakes to contribute in the event of winding up, must also be mentioned.

5. Capital Clause

The amount of share capital with which the company is to be registered and its division into shares of fixed amount are also stated here.

6. Association Clause or Subscription Clause

At least two persons in the case of a private limited company and seven in the case of public limited company must sign the memorandum and agree to take the number of shares shown against their names. Further they also express their desire to form themselves into a company in pursuance to the Memorandum of Association.

4.8 Articles of Association

It is another important document as it contains the rules and regulations for its internal functioning of the company.

4.8.1 Contents of the Articles

The more important contents to be contained in the Articles are listed below

1. The extent to which the regulations in Table A are to be excluded.
2. Adoption or execution of preliminary contracts if any.
3. Share capital, different classes of shares, rights attached thereto, etc.
4. Allotment of shares, calls on shares.
5. Procedure relating to forfeiture of shares and their re-issue.
6. Issue of share certificates and share warrants.

7. Rules regarding transfer of shares and transmission of shares.
8. Conversion of shares into stock.
9. Payment of underwritting commission on shares and debentures.
10. Alteration of share capital.
11. Qualification and remuneration of directors.
12. Borrowing powers of directors.
13. Appointment, qualifications, powers, duties, remuneration, etc of managing director, manager and secretary.
14. Appointment of directors.
15. Rules regarding use of common seal of company, Board meetings and voting rights of members, proxies and polls.
16. Procedure for conducting different kinds of general meetings.
17. Payment of dividends, creation of reserve, etc.
18. Issue of redeemable preference shares, if any.
19. Winding up.

In the case of companies with the liability limited by guarantee, the articles must also state the number of members with which the company is to be registered. It must also state the extent of liability in the event of winding up. In the case of a private company the articles must also contain the following provisions.

a. restricting the right to transfer shares, if any
b. limiting the number of its members to 50 excluding the past and present employee members
c. prohibiting any invitation to the public to subscribe for any shares in or debentures of the company
d. prohibiting any acceptance of deposits from the persons other than the directors, members or their relatives.

4.9 Prospectus

Any document issued by a company inviting the public to buy shares or debentures comes under the definition of prospectus. It serves as a “window through which a prospective investor can look into the soundness of a company’s venture” By going through the information and other particulars, the prospective investors are encouraged to invest in the shares of the company. A private limited company is prohibited from issuing a prospectus.

Distinction between Memorandum and Articles of Association

S.No	Basis of Difference	Memorandum of Association	Articles of Association
1.	Contents	It is the constitution of the company consisting of basic decisions.	It is the bundle of internal rules and regulations of the company.
2.	Relationships	It is the charter of the company indicating the nature of the company and its relationship with the outside world.	It defines the relationship between the members and the management of the company.
3.	Registration	It must be prepared and filed with the Registrar of Companies before the incorporation of the company.	It need not be filed for the purpose of registration. Table 'A' of the companies Act may be adopted if the company's liability is limited by shares.
4.	Alteration	There are strict restrictions on its alteration. Some of the conditions contained in it cannot be altered except with the consent of the company law board.	It can be altered by a special resolution to any extent. But it should not contradict with the Memorandum and the Companies Act.
5.	Violation	Every outsider is expected to know the contents of Memorandum before he enters into contract with the company.	Outsiders are free to assume that the company has fulfilled the formalities mentioned in the Articles.
6.	Nature	It being the charter of the company is the supreme document.	It is subordinate to Memorandum.

CONTENTS OF THE PROSPECTUS

In order to protect the interests of the investors the following points must be given in a prospectus :

1. The main objects of the company.
2. The names, addresses, description and occupations of the signatories to memorandum and the number of shares subscribed by each of them.
3. The kinds of shares with their total numbers and rights attaching to each class of shares.
4. Qualification shares which a member must hold in order to be eligible for election as director. It is fixed by the Articles
5. The names, addresses, descriptions and occupations, the interest, rights and remuneration of the directors, managing directors and the secretaries and treasures.
6. The minimum subscription required for allotment of shares
7. The amount payable along with application and on allotment of each class of shares which is being issued.
8. The time during which subscriptions list will remain open
9. The main points of any contract or proposed contract relating to preferential rights given to shares or debentures of the company.
10. The amount of premium or discount on shares
11. The names of underwriters if any.
12. Particulars about reserves and surpluses.
13. The amount of preliminary expenses .
14. The names and addresses of the auditors.
15. Particulars regarding voting rights at the meetings of the company.
16. A report by the auditors regarding the profits and losses of the company.

4.10. Raising Capital

Shares

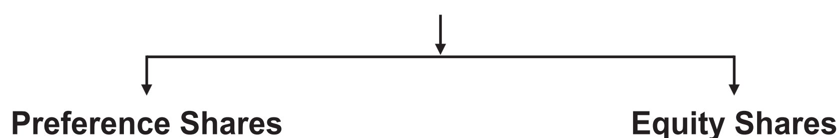
According to section 2(46) of the Companies Act, a share means a share in the share capital of the company and includes stock, except where a distinction between stock and shares is express or implied. A share indicates certain rights and liabilities.

The capital of a company is divided into units of a fixed denomination. Share refers to only such a unit. It is therefore clear that a share is a fractional part of the company's share capital.

4.10.1. Kinds of Shares

According to the Companies Act, 1956 a company can issue only two types of shares viz., 1. Preference shares 2. Equity shares.

4.10. Types of shares



Preference Shares **Equity Shares**

1. Cumulative preference shares.
2. Non-Cumulative preference shares.
3. Participating preference shares.
4. Non - Participating preference shares.
5. Convertible preference shares.
6. Non - Convertible preference shares.
7. Redeemable preference shares.
8. Irredeemable preference share.

I. Preference Shares

The term preference shares focus certain preferential rights over other types of shares. They are,

i). A preferential right to get a fixed rate of dividend during the life of the company. It means that only after payment of dividend to preference shareholders, the surplus, if any, can be used for paying dividend to equity shareholders.

ii). A preferential right to the return of share capital at the time of winding up of the company. This means that when the company goes into liquidation, after discharging debts due to outsiders, the surplus assets must first be used for returning the share capital contributed by the preference shareholders. The remaining surplus alone will be enjoyed by equity shareholders.

Preference shareholders must carry both these preferential rights. However, preference shareholders have certain disabilities. For instance, they do not normally enjoy voting rights. However they get the right to vote.

1. on any resolution affecting their rights
2. on all resolutions when dividend has not been paid to them for certain period as prescribed in the Act.

Kinds of Preference Shares

Preference Shares are of different types based on differing rights.

They are briefly described below.

1. Cumulative Preference Shares

In case dividend is not declared, because of inadequate profit, the right to dividend for that year does not lapse in the case of cumulative preference shares. Dividends not declared and paid get accumulated so that they may be paid out of profits of subsequent years as arrears of dividend before any dividend is paid to equity shareholders.

Preference shares are always cumulative, unless the contrary is expressly stated in the Articles of Association.

2. Non Cumulative Preference Shares

In the case of non cumulative preference shares if dividend is not paid in any particular year, it lapses. Dividend is not allowed to accumulate and such unpaid dividend will not be paid in subsequent years even though sufficient profits are earned.

3. Participating Preference Shares

In addition to the fixed rate of dividend, these shares carry a further right to participate with the equity shareholders in the surplus profits which remain after paying a certain rate of dividend to equity shareholders. Thus they get two kinds of dividend, one fixed rate and the other changing every year depending on the level of excess profits.

Similarly such preference shares have a right to participate in the surplus assets of the company on its winding up after paying in full the preference and equity share capital.

The right to participate in the surplus profits or surplus assets at the time of winding up is available to preference shareholders only if it is specifically expressed in the articles. In other words preference shares are presumed to be non-participating unless specifically stated otherwise in the articles.

4. Non Participating Preference Shares

These shares are entitled to only a fixed rate of dividend. They do not participate either in the surplus or in the surplus assets. In such a case, the entire surplus goes to equity shareholders.

If the articles are silent with regard to this right to participate in the surplus profit or surplus assets, the preference shares will be considered to be only of non-participating type.

5. Convertible Preference Shares

Where preference shares entitle their shareholders to convert their preference shares into equity shares within a specified period, they are known as Convertible Preference Shares.

6. Non-Convertible Preference Shares

Where preference shares cannot be converted into equity shares, they are called non-convertible preference shares. Once issued as preference shares, they continue to be only preference shares throughout the life time of the company without any change in their characteristics. If the Articles are silent regarding this right to convert, the preference shares will be considered to be only Non-Convertible Preference Shares.

7. Redeemable Preference Shares

If the Articles of Association authorise, a company can issue redeemable preference shares. It means, that the capital raised by means of these shares can be returned after a specified period or at any time at its options after giving notice as per terms of issue. These shares can be redeemed either out of profits or out of the proceeds of a fresh issue of shares. Redeemable preference shares can be redeemed if they are fully paid-up. A company cannot convert existing preference shares into redeemable preference shares.

8. Irredeemable Preference Shares

Any preference share that cannot be redeemed during the lifetime of the company is known as irredeemable preference Shares.

II. Equity Shares

Equity shares are those, which are not preference shares. They were also known as ordinary shares. They are entitled to get dividend only after the fixed rate of dividend is paid to preference shareholders. Similarly at the time of winding up of the company, only after returning preference share capital in full, and if there is any surplus, it will be paid to equity shareholders.

The rate of dividend varies from year to year depending on the profits earned by the company. The larger the profits the higher may be the dividend for equity shareholders. In the case of reputed companies, rate of dividend paid to equity shareholders is far higher than the fixed rate paid to preference shareholders. However, when there is no profit in any year, equity shareholders' dividend for that year will not be paid as arrears of dividend in subsequent years even though profits may be very large.

Equity shareholders are entitled to vote on all resolutions.

4.11.1. Allotment of Shares

1. Allotment – Meaning

Allotment means acceptance by a company of the offer made by an applicant to take shares. It is done by the Board of directors by passing resolution to this effect. On allotment the applicant becomes a holder of allotted number of shares.

2. Definition

According to Palmer, "allotment means appropriation to an applicant by a resolution of the directors, of a certain number of shares in response to an application".

3. General Principles regarding allotment:

1. Generally it is a Board of directors, which allot shares, but usually and as per the articles this power is delegated to an allotment committee which should take into account guidelines given by SEBI (Securities Exchange Board of India)
2. Allotment must be done within 3 months from the date of resolution passed by the Board.
3. The fact of allotment is to be properly communicated to the applicant

4. Points to be observed regarding allotment

1. A copy of the prospectus must be filed with the Registrar before its issue to the public.
2. No allotment shall be made unless the amount stated in the prospectus as minimum subscription has been received and the application money on these has been received. Minimum subscription must be received within 90 days from the date of prospectus.
3. Application money received must be kept deposited with a scheduled bank.
4. If minimum subscription is not received within 90 days of the issue of the prospectus, money received on application must be refunded.
5. The company cannot commence allotment until the beginning of the 5th day of the issue of prospectus. This is known as the opening of the subscription list.

5. Irregular Allotment

1. Allotment is considered to be irregular in the following cases. If allotment is made, without receiving at least 5% of the nominal value of shares as application money or
2. Without receiving the minimum subscription within 90 days of the issue of prospectus or

3. If the application money received is not deposited in scheduled bank
4. Where a company does not issue a prospectus because it has made private arrangement for raising capital and if the company has not filed with the Registrar a statement in lieu of prospectus at least three days before the allotment of shares, the allotment becomes irregular.

6. Share Certificate Meaning

Share Certificate is a certificate issued by a company under its common seal signed by one or more of its directors and its secretary, specifying the number of shares held by the named member and showing the distinctive numbers of the shares. It is an evidence of title to the shares. It can be issued even when the shares are partly paid up. A holder of a share certificate is a member of a company enjoying all the rights of membership.

A share certificate discloses

i. The name of the shareholder
ii. The number of shares
iii. Distinctive numbers of the shares
iv. Amount paid up on the value of shares

Share certificate must be issued within three months from the date of allotment of shares.

7. Calls

The usual practice till a few years ago was to collect the value of the share in different stages by way of application money, allotment money and two or three calls. Now-a-days especially when companies of good standing raise capital by issue of shares, the entire share value including premium, if any is collected along with application stage itself. However, we will discuss some of the important features of a call.

8. Call – Definition

The term call refers to “ demand made by a company on its shareholders in pursuance of its articles to pay the whole or part of the balance remaining unpaid on each share after allotment during the lifetime of the company. This means that when a demand is made by a company to pay allotment money, it does not come under call. The demand made for paying the unpaid amount remaining after allotment alone comes under call.

Points to be noted

1. A call can be made only in pursuance of a Board resolution.

2. The resolution must also specify the time before which the call is to be paid and also the amount of the call.

3. At least 14 days' notice must be given for paying the call money.

4. Call can be made at any time during the lifetime of the company and even during the course of winding up. When call is made during the course of winding up it is the official liquidator who makes the call

5. When the call is made it becomes a debt due from the shareholder. On default to pay the call amount, the company can enforce payment with interest.

9. Calls in Advance

A shareholder can pay the whole or part of the amount remaining unpaid on its shares even before a call is made. This voluntary payment is known as calls in advance. This will be adjusted at the time calls are actually made. If the articles authorize, interest on calls in advance can be paid.

10. Forfeiture of Shares Meaning

Forfeiture refers to confiscation of shares held by a member for non-payment of calls due. Once shares are forfeited, the holder of such shares is deprived of the membership of the company and even the amounts already paid on such shares will be retained by the company.

Essentials of a valid forfeiture

To constitute a valid forfeiture

1. The articles must authorise the power to forfeit the shares.

2. Shares can be forfeited only for non-payment of calls due.

3. Shares cannot be forfeited for any other debt due from the shareholder.

4. At least 14 days' notice must be given to the defaulting member for paying the call amount. The notice must also contain a warning that in the event of non-payment, the shares held by him will be forfeited without any further intimation.

5. Shares can be forfeited when the Board passes a resolution, forfeiting the shares

After forfeiture, the name of the shareholder whose shares have been forfeited, will be removed off from the register of members.

11. Reissue of Forfeited Shares

When shares are forfeited they come back to the company, and it has the effect of reducing share capital amount. They become the property of the company. However, such shares can be reissued subsequently.

The forfeited shares can be reissued at a discount. The discount allowed on re-issue should not exceed the amount already collected on such shares.

Forfeited shares can be reissued only by the Board's resolution. The person to whom such forfeited shares are reissued becomes the member of the company and his name must be entered on the register of members.

12. Issue of Shares at a Premium

A company can issue shares at a premium. It means that the issue price can be higher than the face value of the shares. In other words, the difference between the issue price and the face value constitutes share premium. For instance, when a share of the face value of Rs.10 is issued at Rs.12, share premium amount is Rs.2. Share premium is usually collected along with allotment money.

The Companies Act regulates the utilisation of share premium amount only for certain specified purposes such as issue of fully paid bonus shares, writing off preliminary expenses of the company, adjusting it against premium payable on redemption of redeemable preference shares or debentures, etc

13. Issue of Shares at a Discount - Meaning

When shares are issued at a price less than its face value, it is called issue of shares at a discount. When a share of face value of Rs.10 is issued for Rs.8, share is said to be issued at a discount of Rs.2. In other words, the issue price minus the face value of the share forms the discount amount.

Conditions for issuing shares at a discount

1. The shares to be issued at a discount must be of a class already issued. It means a company cannot originally issue shares at a discount. Only subsequent issues can be at a discount.
2. It must be authorised by an ordinary resolution.
3. It should be sanctioned by the Central Government.
4. The resolution must specify the maximum rate of discount at which the shares are to be issued. It should not exceed 10% of nominal value. However higher percentage of discount may be allowed by the Central Government under special circumstances
5. At least one year should have elapsed since the company was entitled to commence business. Shares at a discount must be issued within 2 months from the date of sanction by the Central Government.

4.12 Debentures

The most popular form of borrowing by the company is by way of issuing debentures. Debenture is said to refer to a document, which either creates a debt or acknowledges it.

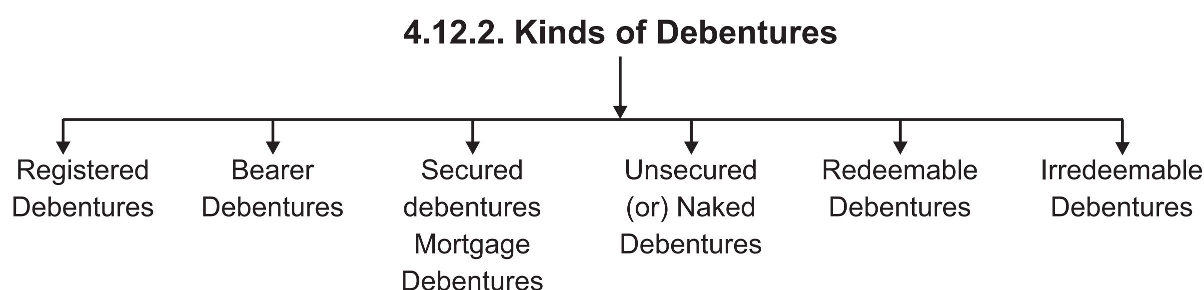
4.12.1 Meaning

The term debenture refers to a document issued by a company acknowledging a debt due by it to its holders. It also provides for payment of interest at a fixed rate at stated intervals. It also contains an undertaking to repay the debt or at its option. It is usually under the common seal of the company.

The debentures must be serially numbered and duly signed by the directors as per the regulations contained in the articles. It should also bear the date of issue and the date of redemption.

4.12.2 Kinds of Debentures

Chart showing kinds of debentures



1. Registered Debentures

Debentures made out in the names of particular persons and whose names appear in the register of debentures are known as registered debentures. They are transferable in the same way as shares. Interest as well as the debenture amount is payable only to the registered holders.

2. Bearer Debentures

Debentures which are payable to bearer and whose names do not appear in the register of debenture holders are known as bearer debentures. Coupons for interest are attached to the document and interest is paid to the holders as it falls due. Bearer debentures are transferable by mere delivery.

3. Secured Debentures or Mortgage Debentures

These debentures are secured by a charge or mortgage on the whole or part of the assets of the company. The charge may be specific or fixed, when a particular asset such as land and building is mortgaged. It is termed as floating charge when it is created on current assets like stock, cash and their values are constantly changing.

4. Unsecured or Naked Debentures

Such debentures which are not secured by any charge on the assets of the company are called unsecured or naked debentures. The holders of these debentures are in the position of unsecured creditors.

5. Redeemable Debentures

Where debentures are to be redeemed (bought back), after a specified period or at the option of the company , they are known as redeemable debentures.

6. Irredeemable or perpetual debentures

This term does not connote that they will never be redeemed. It only indicates that no time limit is fixed for their redemption. However they become repayable

(i) when the company defaults in payment of interest

(ii) when it is wound up

7. Convertible Debentures

These are debentures which give an option to their holders to convert them into equity or preference shares at specified rate of exchange after a certain period. When such debenture holders exercise the right of conversion, they cease to be lenders to the company and become its members. The convertible debentures may be fully convertible or partly convertible.

8. Non- Convertible Debentures

Where no option is given to the holders of such debentures to convert them into preference or equity shares, they are called non- convertible debentures.

4.13. Differences between Shares and Debentures

S.No	Basis of Difference	Shares (Shareholders)	Debentures (Debenture holders)
1.	Rights	Shares represent a part of the share capital of the company	Debentures constitute loan to the company. Debentureholder is only a creditor of the company
2.	Payment of profit	Dividend is paid to the company only when there are adequate profits.	Interest is payable at stated intervals regardless of profit or loss. Directors have no discretion in the matter.

1	2	3	4
3.	Level of profit	While a fixed rate is paid on preference shares, the rate of dividend paid to equity shareholders changes with the level of profits	A fixed rate of interest is payable
4.	Approval	Dividend is payable only when it is recommended by the Board and approved by the general meeting of the shareholders.	The question of getting approval for payment of interest does not arise
5.	Payment of returns	Dividend paid is an appropriation of profit.	Interest paid is a charge on the profit
6.	Liability	The liability of a shareholder is limited to the unpaid amount of the shares	There is no such liability
7.	Issue at discount.	Shares can be issued at a discount only under certain conditions specific in the Companies Act.	There is no such restriction on the issue of debentures at a discount.
8.	Charge on assets.	Shares have no charge on the assets of the company.	Debentures are generally secured
9.	Return of Capital	Shares are non- repayable during the life time of the company except in the case of redeemable perference shares	Debentures are redeemable either at a fixed date or at the option of the company during the lifetime itself.

10.	Participation in meetings.	Shareholders being members of the company are entitled to participate in the company meeting and to vote. They also enjoy other privileges of membership	Debenture holders being only creditors of the company are not entitled to attend such meeting except Debentureholders' meeting.
11.	Repayment of capital	At the time of winding up, share capital will be returned only after claims of all the outsiders including debenture holders are fully met.	Debenture holders have a prior claim over the shareholders even if they are unsecured.

Points to Remember

Joint Stock Company is an association of people who contribute money or money's worth to be employed for a common purpose.

It is an artificial person created by law with a separate legal existence, continuous existence and a common seal

❖ **Features of Joint Stock Company.**

1.It is an artificial person 2. Legal formalities 3. Voluntary association 4. Separate legal entity 5. Perpetual succession 6. Limited liability 7. Large capital requirement 8. Large scale operation 9. Transferability of shares 10. Common seal

❖ **Types of companies.**

1. Chartered Companies 2. Statutory Companies 3. Registered Companies 4.Companies limited by shares 5. Companies limited by guarantee 6. Unlimited Companies 7.Private companies 8. Public Companies 9. Government Companies 10. Foreign Companies 11. Holding Companies 12. Subsidiary Companies

❖ **Differences between a Private and a Public Company**

1.Limit to membership. 2.Use of words in name. 3.Limit to directorship. 4.Prospectus 5. Commencement of Business 6. Transfer of shares 7. Statutory meeting 8. Issue of share warrants 9. Quorum at meetings 10. Allotment of shares 11. Issue of deferred shares 12. Consent of directors 13. Qualification of directors 14. Memorandum and Articles 15. Restriction of directorship 16. Liability of members

❖ **Scope for formation of a Company.**

1. Promotion stage 2. Selecting the name 3. Incorporation stage 4. Capital subscription stage 5. Commencement stage

❖ **Steps in Promotion Stage.**

1. Discovery of a business opportunity 2.Conduct of preliminary investigation 3. Assembling 4. Financing

❖ **Documents to be filed at the time of Incorporation.**

1.Memorandum of Association 2. Articles of Association 3. Written consent of the first Board of Directors of a public Company. 4. Agreement copy with the Secretary 5. Statutory declaration by an advocate, solicitor or a Chartered Accountant that formalities of registration have been complied with. 6. Agreement of Directors to take qualification shares 7. Copy of the prospectus

❖ **Memorandum of Association.**

It is a primary documents to be made by a company Contents of Memorandum of Association

1. Name clause
2. Situation clause or domicile clause
3. Objects clause
4. Liability clause
5. Capital clause
6. Association or Subscription clause

❖ **Articles of Association.**

It is a supplementary document to be prepared by a Joint Stock Company. It contains the rules for internal operation of a company.

❖ **Contents**

1. Amount and classes of capital 2. Adopting preliminary contracts 3. Powers to alter capital 4. Procedure for the conduct of meetings 5. Matter relating to directors 6. Matter relating to accounts and audits 7. Matter relating to dividends, reserves etc 8. Matter relating to secretaries, manager etc 9. Matter relating to the use of common seal 10. Matter relating to winding up of company

❖ **Prospectus**

It is an invitation to the public, to take the shares in it.

❖ **Contents of Prospectus.**

1. Name and address of the company 2.Objects of company 3. Details of shares 4. Details of listing of shares 5. Details of debentures 6. Details of rights of shareholders 7. Details of directors secretary, promoters, bankers, managing agents etc 8. Details of minimum subscription 9. Details of subscription list 10. Details of calls on shares 11. Details of underwriters 12. Details of preliminary expenses 13. Details of reserves and surplus.

❖ **Advantages of Joint stock Company**

1. Huge capital 2. Large scale operation 3. Limited liability 4. Continuity of business 5. Easy transfer of shares 6. Democratic management 7. Availability of credit 8. Easy expansion 9. Better management 10. Government control

❖ **Disadvantages of Joint Stock Company.**

1.Excessive legal formalities 2.Separation of ownership and management 3.Absense of personal touch 4. Delay in decision-making 5.Disunity in management 6.Reckless speculation 7. Neglecting minority interests 8. Greater chances of fraud

QUESTIONS

I. Multiple Choice

Choose the correct answer:

1. Registration of a joint stock company is

   a) compulsory b) optional

   c) compulsory for public limited companies and optional for private limited companies

   d) optional for public limited companies and compulsory for private limited companies

Answer : (a)

2. The minimum number of members for a public limited company is

   a) 2 b) 3 c) 7 d) 10

Answer : (c)

3. The liability of shareholders of a private limited company is limited to

   a) the paid up value of the shares

   b) amount remaining unpaid on the shares

   c) the extent of private assets d) amount called up

Answer : (b)

4. A private limited company can commence business

   a) Immediately on receiving the certificate of incorporation

   b) Only after the certificate of commencement of business is received

   c) On getting name approval from the Registrar

   d) On filing all the documents necessary for formation with the Registrar

Answer : (a)

5. The existence of a company comes to a close

   a) on the death of all its promoters

   b) on death of all the directors of the Board

   c) on transfer of shares by most of its original members

   d) none of the above

Answer : (d)

6. Table A of the Companies Act is a

   a) model minutes book

   b) model form of balance sheet

   c) model of Articles of Association

   d) model of memorandum of association

Answer : (c)

7. Which of the following documents define the scope of a company's activities?

   a) Memorandum of Association b) Articles of Association

   c) Prospectus d) Statutory Declaration

Answer: (a)

8. Which of the following is created by a Special Act of Parliament or in State Assemblies?

   a) Chartered company b) Foreign company

   c) Government company d) Statutory company

Answer : (d)

9. Which of the following companies must file with the Registrar a statement in lieu of prospectus?

   a) a public limited company which raises funds from the public through issue of shares

   b) a public limited company which has made arrangement for racing its capital from directors and their relatives

   c) a private limited company

   (d) all of them

Answer : (b)

10. The minimum subscription specified in the prospectus must be received within

   a) 90 days   b) 120 days   c) 130 days   d) 60 days

Answer : (a)

11. A preference share has priority in

   a) dividend only   b) only in return of capital at the time of winding up

   c) voting rights   d) both dividend and return of capital on winding up

Answer :(d)

12. Shares can be forfeited for

   a) non-payment of any debt due to the company

   b) not attending three annual general meetings consecutively

   c) for non payment of call money

   d). for violent activities at the annual general meetings

Answer : (c)

13. Where the shares are issued at a discount and the nominal value of share is Rs.100, the maximum discount that can be allowed is

   a) Rs.5   b) Rs.10   c) Rs.20   d) Rs.15

Answer : (b)

14. Debenture holders of a company are its

   a) Creditors   b) Members   c) Credit customers

   d) Borrowers

Answer : (a)

15. Debenture holders are entitled to receive interest in the following circumstances

    a) when there are profits

    b) when shareholders also get dividend

    c) every year irrespective of loss

    d) all the above

Answer : (d)

Fill in the blanks with suitable word or words.

1. The minimum of a number of members in a public limited company is _______

2. The liability of a member of a company limited by guarantee is ____________

3. The minimum number of members in a private company is _______________

4. A company, the members of which not less than fifty one percent of the paid-up-share capital is held by a state Government, is known as _________ company.

5. The company, which need not have separate Articles of Association of its own is ______________ company limited by shares.

6. The manner in which the internal management of a company carried on is contained in _________________

7. An advertisement inviting the public to buy the debenture of a public company is known as __________________

8. Preference shares which carry a right to arrear dividend are known as ____________

9. Such shares, as are entitled to a further dividend in addition to the usual fixed rate of dividend are known as ________________ shares.

10. A private company should have at least ______________ directors.

11. The aggregate nominal value of qualification shares shall not exceed ____________ rupees.

12. When a company has issued shares of Rs. 6000 each only, the minimum number of qualification shares that a director should hold is ________________

ANSWER: **1. Seven. 2. Limited. 3. Two. 4. Government. 5. Public. 6. Articles of Association. 7. Prospectus. 8. Cumulative preference share. 9. Participating preference. 10. Two. 11. Five thousand. 12. One.**

III. Match the following

1.	Perpetual succession	a. acknowledgement of debt.
2.	Association clause	b. Table A
3.	Articles of Association	c. continued existence despite change in membership.
4.	Statement in lieu of prospectus	d. situation clause.
5.	Debentures	e. private arrangement of capital.
		f. association not for profit.
		g. subscription clause.

ANSWERS: 1. C, 2. G, 3. B, 4. E, 5. A,

II. Short Questions

1. Define a private limited company.
2. What is a guarantee company ?
3. What do you mean by a Government company ?
4. What is stated in the situation clause in a memorandum ?
5. What does the Articles of Association deal with?
6. For what reasons are shares forfeited ?
7. What is the consequence of not receiving minimum subscription ?
8. Define debentures.
9. What is limited liability ?
10. What is share premium?
11. Mention the documents to be filed for getting the certificate of incorporation.
12. Mention the documents to be filed for getting certificate to commence business after incorporation.
13. What is cumulative preference share?
14. What is meant by perpetual succession?
15. What do you understand by redeemable debentures?
16. What do you mean by issue of shares at a discount?
17. What is the significance of the common seal of the company?

18. What is redeemable preference shares?
19. What are you mean by a foreign company?
20. What do you mean by calls in advance?
21. What do you understand by Promotion of company?
22. What is meant by Reissue of Forfeited shares?

III. Paragraph Questions:

1. Briefly explain the features of the company form of organisation
2. Write a note on Guarantee company.
3. What do you understand by Holding and Subsidiary Companies ?
4. Briefly state the documents to be filed for getting certificate of incorporation.
5. Briefly explain the documents to be filed for getting a certificate to commence business.
6. What is Memorandum of Association? What are its contents ?
7. State briefly the contents of Articles of Association.
8. Write an explanatory note on Redeemable Preference Shares.
9. What are the points to be considered while allotting shares ?
10. Write a note on Irregular Allotment
11. What are the essential conditions of forfeiture of shares ?
12. What are the conditions for issuing shares at a discount ?

IV. Essay Type Questions:

1. Discuss the merits and demerits of company form of organisation.
2. Bring out the distinction between a company and a partnership
3. Discuss briefly the different kinds of companies.
4. Discuss briefly the privileges of a private limited company
5. Explain briefly the procedures to be followed for forming a public limited company.
6. What is prospectus ? State its contents.
7. Explain the different types of shares
8. Explain the different types of debentures.
9. Distinguish between shares and debentures

CHAPTER - 5

JOINT STOCK COMPANIES - II

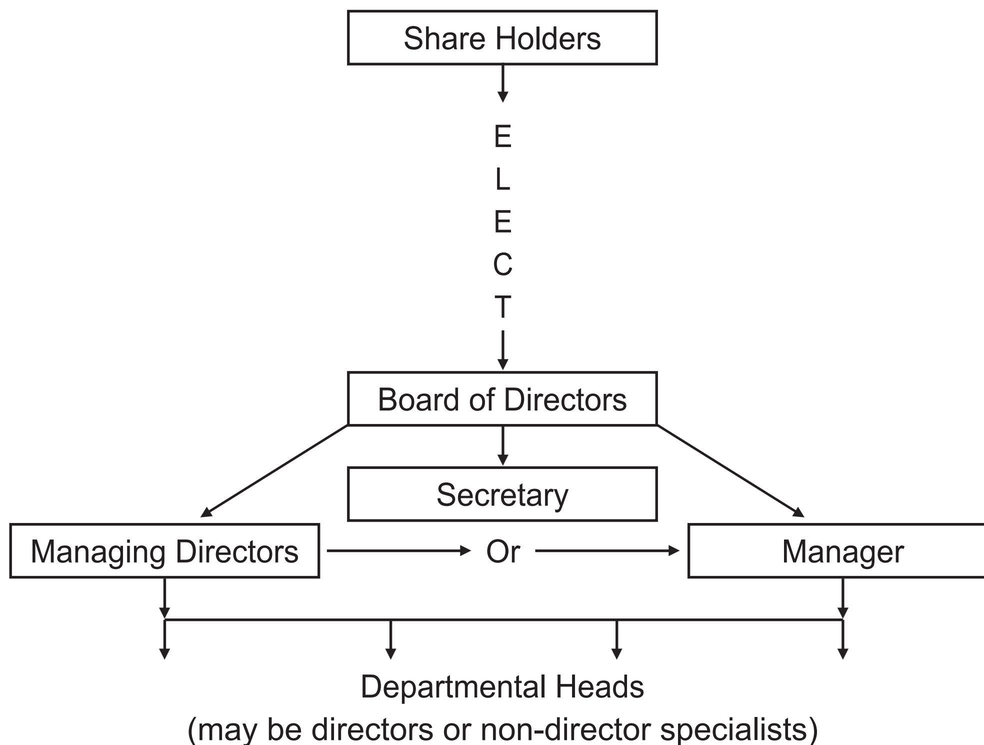
"Only those who can give the best for

the least will survive and others will be for sale"

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 5.1. Company management – Directors – Qualifications – Disqualifications
- ❖ 5.2. Appointment of Directors – Removal – Vacation of office – Powers of Directors
- ❖ 5.3. Duties – Liabilities – Civil and Criminal liabilities
- ❖ 5.4. Managing Director – Meaning – Manager – Managerial Remuneration
- ❖ 5.5. Company Secretary – Definition – Importance of Secretary – functions and duties of Secretary.
- ❖ 5.6. Meetings – Meaning – Kinds – Proxy – Quorum – Agenda
- ❖ 5.7. Resolutions – Meaning – Kinds – Voting – Minutes.

STRUCTURE OF THE COMPANY MANAGEMENT



5. 1. COMPANY MANAGEMENT

Management of the affairs of the company is entrusted to Board of directors who are elected by the shareholders. Though shareholders are the real owners of the company, they cannot take part directly in its management. However, there is indirect participation as it is in the hands of the elected representatives called directors.

5.1.1 Position of Directors

1. Directors as agents

When the directors enter into contract with third parties, sign documents for and on behalf of the company etc. they act as the agent of the company. They bind the company by their acts.

2. Directors as Trustees

They are in the position of trustees, when they manage the assets and properties of the company. Similarly when they exercise the powers entrusted to them they are in the same position. It means that they should safeguard the interest of the company and should never abuse the powers for promoting their personal ends.

3. Directors as Officers

Directors also act as officers of the company. When they have to manage the affairs of the company, they are in the position of Chief Executive Officers.

Thus the directors combine in themselves the roles of agents, trustees and officers.

5.1.2. Qualifications of Directors

1. Only individuals can be appointed as directors of the company.
2. They must have contractual capacity.
3. They must possess qualification shares, if laid down in the Articles. In such a case the qualification must be acquired within two months of their appointment as directors. The nominal value of qualification share should not exceed Rs.5000 or one share where its nominal value exceeds Rs.5000.

5.1.3. Disqualifications of Directors

The following persons are disqualified for appointment as directors of a company.

1. A person of unsound mind
2. An undischarged insolvent
3. Any person who has applied for being adjudged an insolvent
4. Any person who had been sentenced with imprisonment for an offence involving moral turpitude for a period exceeding 6 months and a period of 5 years has not elapsed since the date of expiry of the sentence
5. A person who has not paid the call money and the calls in arrear are outstanding for more than 6 months
6. Any person disqualified by a court for appointment as director for having committed fraud in management

5.2. APPOINTMENT OF DIRECTORS

First directors are usually named in the Articles. If the Articles are silent, the signatories to the memorandum shall be deemed to be the first directors of the company.

a. Appointment of Directors by the Company

Subsequent directors are elected by shareholders at the Annual General Meetings. If a company adopts the principle of retirement by rotation, one-third of the directors must retire by rotation. The retiring directors are eligible for reappointment.

b. Appointment by Board of directors

The Board can appoint additional directors. They can fill up casual vacancy caused by death, resignation, etc. They can also appoint alternate director. If empowered by Articles, the Board may appoint an alternate director during his absence for a period of not less than 3 months from the date in which meetings of the Board are ordinarily held.

c. Appointment by Third Parties

If authorised by the Articles, third parties such as vendor of the business, banking or financial institutions which have advanced loans to the companies, can appoint their nominees on the Board.

d. Appointment by Central Government

The Central Government can also appoint directors on an order passed by the Company Law Board or on the application of not less than 100 members of the company or of members holding 10% of the total voting power.

Number of Directorship

A person can hold office as director in not more than 15 companies at the same time. In calculating the number of directorships, the directorship of independent private limited companies, non-profit associations, and alternate directorships are excluded.

5.2.2. Removal of Directors

A director can be removed from office by the company by an ordinary resolution before the expiry of his term, when such a director has acted in fraudulent manner or abused his fiduciary position.

The Central Government can remove a director under certain circumstances.

The Company Law Tribunal may also order for removal of a director where an application has been made to it on charges of oppression and mismanagement of the company's affairs.

5.2.3 Vacation of Office

A director must vacate his office in the following circumstances.

i. When he is found to be of unsound mind by a competent court

ii. If he is adjudged an insolvent

iii. If he fails to obtain his qualification shares within the prescribed time or ceases to hold at any time thereafter

iv. If he is convicted of an offence involving moral turpitude and sentenced to imprisonment for not less than 6 months

v. If he fails to pay any call money within 6 months

vi. If he absents himself from three consecutive Board meetings or from all the meetings of the Board for a continuous period of three months whichever is longer without obtaining leave of absence from the Board

vii. If he becomes disqualified by an order of the court

viii. If he fails to disclose to the Board his interest in any contract entered into by the company

5.2.4. Powers of Directors

1. General Powers

The Board of directors of a company is entitled to exercise all such powers and to do all such acts and things as the company is authorised to do. However the Board shall not do any act which is to be done by the company in general meeting.

2. Statutory Powers

By means of resolutions passed at the Board meetings, the following powers can be exercised by the directors:

i. To make calls

ii. To issue debentures

iii. To borrow money otherwise than on debentures

iv. To invest the funds of the company

v. To make loans

3. Other Powers to be exercised at Board Meetings

i. To fill up casual vacancy in the office of directors

ii. To appoint additional directors, if authorised by the articles

iii. To appoint an alternate director if authorised by the articles

iv. To accord sanction to contracts in which any director or his relative is interested

v. To recommend a certain rate of dividend to be declared at the annual general meeting

vi. To make investments in the companies in the same group

vii. To appoint the first auditors of the company

viii. To fill up the casual vacancy in the office of an auditor not caused by resignation

4. Restrictions on the powers of directors

The following powers cannot be exercised by the Board without the consent of the shareholders in the general meeting.

i. To sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company

ii. To extend time for repayment of any debt due by a director

iii. To borrow money where the money to be borrowed together with that already borrowed is in excess of the aggregate of the paid up capital and free reserves

iv. To contribute to charitable funds in excess of the prescribed limit

5.3. DUTIES

1. General Duties

1. Duty of good faith: They must act bona fide in the interest of the company. They should not make any secret profits.
2. Duty of reasonable care: They must discharge their duties with care and diligence.
3. They must attend the Board meeting regularly.
4. Duty not to delegate: They must perform the duties personally. They can delegate only certain functions as permitted by the articles.

2. Statutory Duties

Some of the important duties laid down in the Companies Act are listed below.

1. To sign a prospectus and deliver it to the Registrar before its issue to the public.
2. To see that all moneys received from applicants for shares are kept in a scheduled bank.
3. Not to allot shares before receiving minimum subscription.
4. To forward a statutory report to all its members at least 21 days before the date of the meeting.
5. To hold the meetings at least once in three months.
6. If a director is interested in a contract, to disclose the nature of his interest.
7. To call for annual general meeting every year.
8. To file all statutory returns with prescribed authorities.
9. To take steps for filing declaration of solvency in the case of voluntary winding up.

5.3.3. LIABILITIES OF DIRECTORS

A. Civil Liabilities

1. Liabilities to Third Parties: They are liable to third parties,

1. when they enter into contracts which are beyond the powers of memorandum.
2. for misstatement in the prospectus.
3. when they enter into contract in their own names.

2. Liability to the company: They are liable to the company,

1. for gross negligence in the performance of their duties.
2. for breach of trust.
3. when they fail to act honestly in the interest of the company
4. for misfeasance.
5. for fraudulent conduct of the business.

B. Criminal Liability

Directors may incur criminal liability for the following activities.

1. Misstatement in the prospectus.
2. Failure to file Return of Allotment.
3. Failure to issue share certificates within the prescribed period.
4. Failure to pay dividend within 42 days from the date of declaration.
5. Failure to lay before the Annual General Meeting audited profit and loss account and balance sheet.
6. Failure to furnish the necessary information to the company’s auditors.
7. Failure to file copies of special resolutions with the Registrar within 30 days of passing the resolution.
8. Destruction of important documents.
9. Holding the office of directors in more than 15 companies excluding private companies.

5.4. MANAGING DIRECTOR

Meaning

Managing Director is a director who is entrusted with substantial powers of management, which would not be otherwise available to him. Routine administrative

work is not included in the term “Substantial Powers of Management”. A managing director is appointed

a) as result of an agreement entered into with the company or

b) as a result of a provision contained in the memorandum or articles or

c) in pursuance of a resolution passed either by the Board or by the company in general meeting

Some of the important points worth noting regarding managing director are given below.

1. Without the approval of Central Government no change can be effected in the terms of appointment of a managing director.
2. A managing director cannot be appointed for a period exceeding 5 years at a time.
3. A person cannot act as a managing director of more than 2 companies at a time.
4. The remuneration should not exceed 5% of the annual net profits if there is one managing director. If there is more than one such director, 10% for all of them together. This can be paid by way of monthly payment or at a specified percentage of net profits or by both ways.

5.4.2. Manager

Managers and managing directors have similar functions to perform. The important difference between the two is that while a managing director must be a director, a manager need not be a director. Only an individual can be appointed as a manager.

Subject to the superintendence, control and direction of the Board of directors, a manager is entrusted with the management of the whole or substantially the whole of the affairs of the company.

1. A company cannot have more than one manager.
2. The powers of a manger are wider than those of a managing director, because the manager may be entrusted with the management of whole of the affairs of the company.
3. Maximum remuneration payable to a manager cannot exceed 5% of the annual net profit.
4. Manager cannot be appointed for a period exceeding 5 years at a time.

5.4.2. Managerial Remuneration

Managerial remuneration may take the form of monthly payments (salary), or a specified percentage of net profits or a commission, etc. This expression shall include the value of perquisites. The total managerial remuneration payable by a public limited company to its director or manager must not exceed 11% of the net profits of the company for that financial year. Remuneration to a managing director or whole time director may be paid not exceeding 5% of the net profits and if there is more than one such director, 10% for all of them together.

In a year of no profits or inadequate profits, such managerial remuneration shall be governed by the provisions of Schedule XIII to the Companies Act.

5.5 COMPANY SECRETRARY

Definition

According to the Companies Act " a company secretary means company secretary as defined under the Company Secretaries Act and includes any other individual possessing the prescribed qualifications and appointed to perform the duties by a secretary under this Act or any other ministerial or administrative duties".

According to the Company Secretaries Act, 1980 a company secretary is a person who is a member of the Institute of Company Secretaries of India.

1. The importance of company secretary: As an officer of great importance, a secretary has extensive duties and responsibilities. The success of the company depends upon his efficient functioning and capacity for quick grasp of complicated situtation.

1. Though he is chiefly concerned with the implementation of the policy framed by the company, he has authority to do many important things on behalf of the company. Though he is not an agent of the company, he is entitled to sign the contracts concerned with the administrative side of a company's affairs.

2. With growing industrialisation the company administration has become more and more complex. Various legislative enactments which have bearing on a company's functioning require a thorough understanding of law, accountancy, management, industrial relations, and the multitude of other aspects affecting administration. This has significantly changed the role and importance of company secretary. Hence the Companies Act has made it obligatory for every company having a paid up capital of Rs.50 lakh or more to appoint a duly qualified company secretary.

3. The importance of the role of a secretary also becomes clear when it is noted that Income Tax Act, 1961 and various other Acts consider the secretary to be the principal officer of the company. He is in fact the Chief Executive Officer and the principal co-ordinator.

4. Most of the important things are carried out only through resolutions passed at the Board meetings and other meetings of the company. It is the secretary who makes the spade work for the successful conduct of any meeting.

5. He also acts as a spokesperson of the company, raising its image and reputation of the company through his personality, integrity, time sense and knowledge of business.

6. As an agent of the Board of directors, he serves as a link between the Board on the one hand and the staff, shareholders and customers on the other hand. Through his initiative, drive and enthusiasm, he removes misunderstandings and builds up smooth relationship.

The problems of giant companies of today are more complicated and the problems assume enormous proportions. While the services of a number of specialists are available to attend to this problem, it is the company secretary with his alround expertise to co-ordinate the various activities ensures the smooth and successful functioning of the company. The company secretary is undoubtedly the pivot around which revolves the corporate machinery.

2. Functions and Duties of a Company Secretary

1. As a head of the Secretarial department, the secretary controls and supervises the activities of the department under his control. As a principal officer of the company, he signs documents requiring authentication. He performs all such acts as authorised by the Board.

2. The secretary arranges for the Board meeting, in consultation with the chairman of the Board, fixes a day, place and time of the meeting and prepares agenda and issues the notices of meetings.

3. He ensures that the actions of the Board do not infringe the provisions of the Companies Act and are not beyond the scope of Memorandum and Articles of association.

4. The secretary functions in the best interest of the shareholders. He has to deal with the shareholders with tact. He performs all legal formalities connected with the conduct of general meetings of shareholders and records the proceedings of the minutes in the Minute book. He should ensure that all correspondence with shareholders is dealt with promptly and their queries answered carefully keeping in view the statutory provisions in this regard.

5. His functions in relation to issue of allotment letters, share certificates, dividend warrants, share transfers, forfeiture of shares and a host of other things are also important.

6. As a chief officer closely connected with the Board, he has to co-ordinate the work of different departments.

7. He has to liaise between staff and directors, management and labour and other persons dealing with the company efficiently and effectively.
8. He has to inspire confidence in their staff and win their co-operation.

3. Statutory Duties

1. To sign any document requiring authentication under any statute
2. To arrange for filing statement in lieu of prospectus
3. To deliver share or debenture certificate within 3 months of allotment or within 2 months of registration of transfer
4. To file notice of situation of the registered office of the company
5. To make a statutory declaration for getting the certificate of commencement of business and file it with the Registrar
6. To sign the annual return
7. To send notices of general meetings to every member of the company
8. To prepare minutes of every general and Board meetings or meetings of every committee of the Board within 30 days.
9. To maintain a number of statutory books such as register of members, register of debenture holders, etc.,

4. General Duties

1. To discharge his duties most diligently and honestly and not to act beyond the scope of his authorities.
2. To maintain secrecy of confidential matters

5.6 MEETINGS

A company as a legal entity is capable of acting in its own name. But since it has no physical existence, it has always to act only through its members or directors of a company. Only when they act as a body at the respective meetings through resolutions, the company is perceived to be acting. Hence the meetings are very important for transacting business and implementation of business policies.

1. Meeting: Meaning

An assembly of relevant persons validly convened through proper notice for transacting business mentioned in an agenda is known as a meeting.

Requisites of a valid meeting:

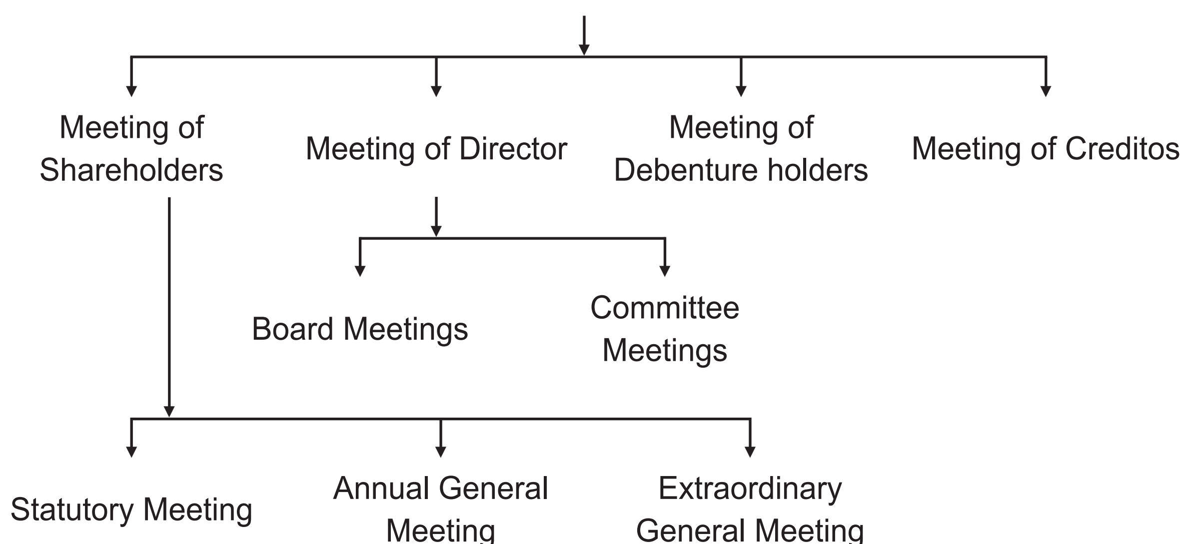
A meeting of any kind, to be valid, must satisfy the following conditions.

1. It must be properly convened. That is, it should be called by the proper authority entitled to call the meeting. The proper authority to convene the meeting is the Board of directors, shareholders or the Company Law Board.
2. It must be legally constituted. This means that the meeting should have a proper chairman ; quorum must be present.
3. It should be conducted according to the provisions of the Act and the Articles.
4. It should be properly conducted.

Kinds of company meetings

Let us briefly discuss meetings of shareholders, Board of directors, creditors and debenture holders in this chapter.

5.6.2 KINDS OF COMPANY MEETINGS



5.6 MEETINGS OF SHAREHOLDERS

1. Statutory Meeting

The first meeting of the shareholders of a public limited company which is mandatory as per the Companies Act is known as statutory meeting. Every public limited company limited by shares and a guarantee company must compulsorily hold this meeting within 6 months and not earlier than one month from the date on which the company is entitled to commence business. This is held only once in the life time of the company.

The object of the meeting is to afford an opportunity to the shareholders to know important details of company formation, the success of its capital issue, properties that have been acquired, etc. Along with the notice convening the meeting, a report called statutory report must also be sent to all the members at least 21 days before the date of the meeting.

This meeting provides an opportunity to members to discuss various matters relating to the contents of statutory report. They can also effect any modification to the contracts mentioned in the prospectus.

2. Statutory Report

This report sets out the following.

1. Details of shares issued for cash and those issued for consideration other than cash
2. Total amount of cash received on account of shares and other sources
3. An abstract of receipts and payments upto a date within 7 days of the report
4. An account or an estimate of the preliminary expenses
5. Particulars of contracts for approval and proposed modifications
6. Details of underwriting contract not carried out and the reasons therefor.
7. Particulars of commission or brokerage paid or to be paid to directors on issue of shares or debentures
8. Particulars about directors, managing directors, manager and secretary
9. Particulars of calls due from directors, managing director, etc

The statutory report must be certified as correct by at least two directors, one of whom must be a Managing Director. As far cash received on shares allotted and other receipts and payments, they must be certified by an auditor. A certified copy of the statutory report must be filed with the Registrar. Members can inspect the list of members and the number of shares held by them.

Consequence of default

If any default is made in holding the statutory meeting, within the prescribed time or in filing the statutory report to the Registrar, every director or other officer in default is punishable with a fine upto Rs.5000.

Further the court can order even winding up of the company on a petition filed by a member of the company.

Such is the significance of the statutory meeting.

2. Annual General Meeting

Every company is required to hold an annual general meeting in addition to any other meetings.

The first annual general meeting must be held within a period of 18 months from the date of its incorporation. Subsequently the interval between two annual general meetings must not be more than 15 months.

The ordinary business at this meeting are:

i. Consideration and adoption of the annual accounts and the reports of the directors and auditors

ii. Declaration of dividend

iii. Appointment of directors in place of those retiring

iv. Appointment of auditors and fixing remuneration to them

Special business All other businesses transacted at this meeting are called special businesses. Examples of special business: Removal of a director, issue of rights or bonus shares, election of a person other than a retiring person as a director, etc

Consequences of Default

If a company fails to hold an annual general meeting, the company and every officer who is in default shall be punishable with a fine upto Rs.50000 and in the case of continuing default, with a further fine of Rs.2500 per day during which the default continues.

Importance of Annual General Meeting

The shareholders get an opportunity to review the performance of the company to discuss the affairs of the company and to take steps necessary for protecting their interests.

3. Extraordinary General Meeting

Meaning:

Any meeting other than the statutory meeting and the annual general meeting of the company is called extraordinary general meeting. It is convened for transacting any urgent or special business which cannot be postponed till the next annual general meeting. An extraordinary general meeting may be convened by the Board of directors on its own, or on the requisition of the members subject to certain conditions.

Extraordinary General Meeting convened by the requisitionists:

If the Board of directors fails to call the meeting within 21 days and the meeting is not held within 45 days of requisition, the requisitionists themselves may call the meeting within three months of the date of requisition.

Extraordinary General Meeting by Company Law Board:

If it is not possible for the members to convene an extraordinary meeting, the Company Law Board either on its own motion or on the application of any director or member may call such a meeting.

4. Meetings of the Board of Directors

Meetings of directors are called Board meetings. They are very important because all important matters relating to the company and its policies are decided thereat.

Provisions regarding Board meetings:

The Board meeting must be held at least once in every three- calendar months. At least four such meetings should be held in every year.

The notice of every Board meeting must be given in writing to every director who is present in India at his usual address. The quorum for the Board meeting shall be one third of the total strength of the Board (any fraction being rounded off as one) or two directors whichever is higher.

The Board is entitled to exercise all such powers and to do all such acts as the company is authorised to do. However the Companies Act imposes certain restrictions on the powers of the Board.

5. Meetings of Committee of Directors

Since it is not possible for the Board to devote time to carry on investigation on different matters, the Board may delegate their powers to committees, if the Articles of Association so provides.

The Board is empowered to delegate for example the following powers to any committee of directors.

i. The power to borrow money, otherwise than on demand.

ii. The power to invest the funds of the company.

iii. The power to make loans, etc.

6. Meetings of Debenture holders

Such meetings are convened when the company wants to change the terms of security or to modify the rights, or to change the rate of interest payable, etc

7. Meetings of the Creditors

Meetings of creditors are held when the company proposes to make a scheme of arrangements with its creditors.

a. Proxies

The term 'proxy' may refer to a person who is authorised by a member for the purpose of attending a meeting. It also means the instrument by which the proxy is authorised. The following points relating to proxies are worth noting:

i. Members of a company having a share capital have a right to appoint proxies.

ii. Proxy need not be a member of the company.

iii. Proxy can attend a meeting but he has no right to speak.

iv. Proxy cannot vote except on a poll.

v. A member can appoint more than one proxy.

vi. The proxy form must be in writing, duly signed by the appointer and stamped. It must be lodged at the company's office 48 hours before the commencement of the meeting.

b. Quorum

The word 'quorum' means the minimum number of members required to be personally present at a meeting for validly transacting any business. Usually the quorum is fixed by the Articles.

The quorum shall be two members personally present in the case of a private company and five in the case of public company. The quorum for the Board meeting shall be one third of the strength (any fraction to be rounded off to one) or two directors whichever is higher. However the Articles may provide a larger number.

For calculating quorum, proxies should not be counted and only members present in person must be considered.

Quorum should be present throughout the meeting. The importance of quorum can be understood if it is noted that any resolution passed in the absence of a quorum is not valid. Similarly if quorum is not present, the meeting itself stands adjourned.

c. Agenda

Agenda means the list of business to be transacted at the meeting. It is generally prepared by the secretary in consultation with the chairman.

5.7. RESOLUTIONS AND MINUTES

5.7.1. Resolution: Meaning

When a proposal placed before the meeting is passed by the meeting, it becomes a resolution. A resolution thus reflects the decision of the majority.

5.7.2. Kinds of resolutions

They are of three types:

1. Ordinary Resolution
2. Special Resolution
3. Resolution requiring special notice.

1. Ordinary Resolution Any resolution passed by a simple majority is an ordinary resolution. Simple majority means that 51 per cent or more of the votes have been cast in favour of the resolution.

Some of the items requiring ordinary resolution

a. Adoption of audited accounts, Directors' report and Auditors' report.

b. Appointment of auditors

c. Election of directors in place of those retiring

d. Declaration of dividend.

e. Issuing shares at a discount

f. Removing a director before the expiry of his term

g. Appointing a director in the place of removed director.

2. Special Resolution

Special resolution is one which is required for transacting any special business. It has to be passed by a three-fourths majority. In other words, the votes cast in favour of the resolution must exceed three times the votes cast against it.

The notice calling the meeting should specify the intention to pass the resolution as a special resolution. Notice must be given at least 21 days before the date of the meeting.

Some of the items requiring special resolution

1. Altering the objects clause of the memorandum.
2. Changing the place of the registered office from one State to another.
3. Altering the Articles of Association.
4. Reducing share capital.
5. Making loans to other companies under the same management.
6. Paying interest out of capital in certain cases.
7. Voluntary winding up of the company.

3. Resolution requiring special notice

This type of resolution does not belong to a separate category. It can be either an ordinary resolution or a special resolution. However, the mover of the proposed resolution must give a special notice of 14 days to the company. On receipt of this resolution, the company in turn has to give notice to the members atleast 7days before the date of the meeting. Where it is not practicable, it can publish it in a newspaper.

Items requiring special notice

1. Appointing an auditor other than a retiring auditor.
2. Passing a resolution that a retiring auditor should not be appointed.
3. Removing a director before the expiry of his term.
4. Appointing a director in place of the removed director.

5.7.3. Voting and Poll

Voting

Voting means expressing one's intention either for or against a proposed resolution, called motion. In a company meeting voting can be by way of acclamation of voice, show of hands, and poll.

1. Voting by acclamation of voice: Those favouring the motion are requested to say 'aeys' (yes) or those who are against it are requested to say 'nays' (no).The intention of the members is ascertained by the volume of sound.

2. Voting by show of hands: Members favouring a resolution are asked to raise their hands and the number is counted. Similar procedure is adopted to count the number of members who are against it. Thus the resolution is declared passed or lost.

3. Voting by Poll: When dissatisfied with the result of voting by show of hands, a poll may be demanded. Here each member records his vote on a voting card for or against the resolution. The voting rights of a member are in proportion to his share of the paid up equity capital of the company.

Either the chairman on his own motion or on demand by prescribed number of members present in person or by proxies, can order poll. Proxy is allowed to vote in a poll.

5.7.4 MINUTES

The term minutes refers to accurate official record of decisions taken at various company meetings. Every company must keep the minutes containing summary of all proceedings of general and Board meetings in books .Minutes should be brief and factual. It should be so accurate as not to give room for misinterpretation. It should be free from superfluous words.

The following particulars should be present in the minutes.

i. Nature of meeting – Annual General, Extraordinary, Board, etc
ii. Date, time and place of meeting
iii. Names of chairman, directors, secretary, and number of members attending
iv. Business of the meeting in the order set out in the agenda

v. Approval of the minutes of the last meeting
vi. Resolutions passed in the meeting
vii. Chairman's signature with date

Points to Remember

Management of the affair's of the company is entrusted to a Board of Directors who are elected by the shareholder.

Position of Directors.

1. Directors as agents 2. Directors as Trustees 3. Directors as officers

Appointment of Directors

a. By the company b. By Board of Directors c. By Third parties

d. By Central Government

Powers Directors.

a. General powers b. statutory powers and other powers

Duties of Directors

a. General duties b. Statutory Duties

Liabilities of Directors

a. civil liabilities b. criminal liabilities

Meetings

1. Meetings of shareholders

a. Statutory Meeting b. Annual General Meeting

c. Extraordinary General Meeting

2. Meetings of Directors

a. Meetings of Board of Directors b. Meetings of the Committee of Directors

c. Meetings of Debentures holders d. Meetings of Creditors

Resolutions

1. Ordinary resolution
2. Special resolution
3. Resolution requiring special notice

QUESTIONS

I. Multiple Choice Questions

Choose the correct answer:

1. First directors are appointed by

   a) members in statutory meeting

   b) members in the first Annual General meeting

   c) by being named in the Articles of Association

   d) Registrar of Companies

Answer : (c)

2. A director is acting as

   a) agent of the company

   b) trustee of the company

   c) chief executive officer of the company

   d) all of these

Answer : (d)

3. A person can hold directorship of not more than __________ public limited companies

   a) 10 b) 15 c) 20 d) limitless

Answer : (b)

4. The value of qualification shares of a director in a public limited company shall not exceed

   a) Rs.5000 b) Rs.5,00,000 c) Rs.50,000 d) Rs.500

Answer : (a)

5. The overall maximum managerial remuneration in a public limited company shall not exceed

   a) 11% of net profits

   b) 11% of paid up capital and free reserves

   c) 5% of net profits

   d) 5% of paid up capital and free reserves

Answer : (a)

6. A company secretary is appointed by

   a) Government

   b) The Institute of Company Secretaries of India

   c) The Board of Directors

   d) Shareholders in Annual General Meetings

Answer : (c)

7. A company should compulsorily appoint a qualified company secretary, having a paid up capital of more than

   a) Rs. 5 Lakh b) Rs.50 Lakh

   c) Rs.25 Lakh d) Rs.15 Lakh

Answer : (b)

8. Which of the following must hold a statutory meeting ?

   a) Statutory Companies b) Private Limited Companies

   c) Public Limited Companies d) Chartered Companies

Answer : (c)

9. The interval between two annual general meetings shall not exceed

   (a) 15 months (b) 12 months

   (c) 18 months (d) 20 months

Answer : (a)

10. Which of the following business is not transacted at the Annual General Meeting

   a) appointment of auditors b) issue of debentures

   c) appointment of directors in place of those retiring

   d) declaration of dividend

Answer : (b)

11. Who can call Extraordinary General Meeting ?

   a) Company Law Tribunal

   b) Board of Directors on its own or on the requisition of members

   c) By the requisitionists themselves on Board's failure to convene

   d) all of these

Answer : (d)

II. Fill up the blanks with suitable word or words

1. Directors act as _______________ trustess and officers of the company
2. The share holders are the real _________________ of the company
3. First directors are usually named in the_________________
4. Statutory meeting must be held not later than_________________ and not earlier than _____________ from the date on which a public company is entitled to commence business
5. A statutory report must be sent to every member of the company atleast ______ days before the meeting is to be held.
6. The time between two consecutive annual general meetings should not exceed _________________ months.
7. Altering the Articles of Association requires ________________ Resolution
8. A person Appointed to attend a meeting on behalf of a share holder is known as___________________
9. The Quorum for a General Meeting of members of a public company is_________________
10. The minimum number of members required for a meeting is known as__________________
11. Auditors are generally appointed and their remuneration, fixed at the _________________ meeting.
12. The notice calling the annual general meeting, must, be given to all its members at least _________________ days before the date of the meeting.

Answer

1. Agents	7. Special
2. Owners	8. Proxy
3. Articles of association	9. Five
4. Six months, One month	10.Quorum
5. 21	11. Annual General Meeting
6. 15	12. 21

III. Match the following

1.	Minutes	a. Minimum number of members necessary for a meeting
2.	Ordinary resolution	b. A person appointed to attend a meeting on behalf of a member
3.	Quorum	c. Record of the proceedings of a meeting
4.	Proxy	d. Proposal placed before a meeting
5.	Motion	e. Supported by a simple majority
		f. Supported by three-fourths majority
		g. notice of twenty – one days

(Ans: 1 – c, 2 – e, 3 – a, 4 – b, 5 – d)

IV. Short Answer Questions.

1. Mention the methods in which directors are appointed.
2. What is a statutory meeting?
3. What is statutory report?
4. When is Extraordinary General Meeting convened ?
5. Who can convene Extraordinary General Meeting ?
6. What is proxy?
7. What do you mean by quorum?
8. What is an agenda?
9. What is “Minutes”?
10. What usual business is done at an Annual General Meeting?
11. Is there any special qualification prescribed for a company director?
12. Who is an alternate director?
13. What is meant by resolutions requiring special notice?
14. What is a special resolution?
15. What do you mean by poll?
16. How is the voting right in a company exercised?

V. Paragraph Questions.

1. Explain the position of a director in a company
2. What are the disqualifications for a director?
3. How are directors appointed in a public limited company ?
4. State the circumstances in which a director can be removed?
5. State the circumstances in which a director vacates his office.
6. Write an explanatory note on Managing director
7. Write an explanatory note on Manager
8. State the differences between Managing director and Manager
9. Write a short note on Managerial Remuneration.
10. What are the requisites of a valid meeting?
11. Enumerate the contents of a statutory report.
12. Write notes on Extraordinary General Meeting.
13. Write notes on Annual General Meeting.

VI. Essay Type Questions

1. Discuss the powers of directors and restrictions placed on them.
2. Briefly explain the functions and duties of directors.
3. Bring out the significant role of a company secretary.
4. Discuss the functions and duties of a company secretary.
5. What is a statutory meeting? List out the contents of a statutory report.
6. Write explanatory notes on

   a) Annual General Meeting b) Board Meeting

   c) Extraordinary General Meeting
7. Discuss the different types of resolutions that can be passed in the meetings of a public limited company and the business transacted in each category.
8. Write explanatory notes on

   a) Proxy b) Quorum c) Minutes

CHAPTER - 6
STOCK EXCHANGE

"Old is Gold-New is Platinum"

Learning Objectives :

After reading this chapter you will be able to learn the following.

- ❖ 6.1. Introduction-Primary and Secondary market
- ❖ 6.2. Procedures regarding new issues
- ❖ 6.3. Stock exchange-Characteristics- Functions-Benefits- Limitations.
- ❖ 6.4. Investors and Speculators - Differences-Kinds
- ❖ 6.5. SEBI Features-Objectives-Functions-Powers
- ❖ 6.6. Mutual funds-Meaning-Advantages.
- ❖ 6.7. Bombay on-line trading (BOLT)

6.1. INTRODUCTION

The increased needs of trade, commerce and the society in the past, necessitated the establishment of large scale enterprises. The present trend of industrial enterprises is to increase their size through expansion and diversification. Large scale undertakings are organised in the form of joint stock companies. To meet its enormous capital requirements, the companies rely on individual and

institutional investors. The capital (long term) required by the company is divided into small units of fixed amount. These units are called 'Shares'. Companies issue these shares to the public to raise owned capital i.e., shares represent ownership interest. Additional capital required for medium and short period, can be raised by the company through debentures. The debenture is an acknowledgement for raising loan from the public, by the company. Debentures denote creditorship interest.

SECURITIES

A 'security' means a certificate or document indicating either ownership interest (share) or creditorship interest (debenture).

Securities may include

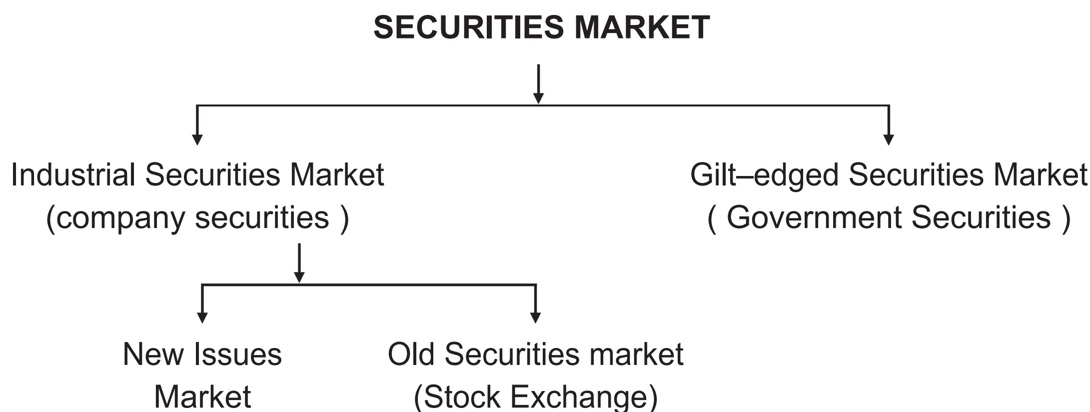
1. Company securities – shares, stocks, bonds, debentures.
2. Government securities.

SECURITIES MARKET

Securities market refers to both the place and the persons who deal with securities. It includes buyers and sellers of securities and agencies/institutions which help in the buying and selling of securities of companies and government.

Securities market may be classified into two categories.

1. Primary market.
2. Secondary market.



Primary market is concerned with issue of new shares. Secondary market deals with resale of securities traded in primary market.

PRIMARY MARKET (New issues market)

'Primary market' denotes the market for new issues. It has no physical existence. It is concerned with the floatation and issue of new shares and debentures by new or existing companies. The shares are offered to the public.

The primary market establishes a linkage between the companies raising finance and the investing public. To make new issues, companies are assisted by brokers, underwriters or commercial banks, in general. The public, who are interested in subscribing for the shares of the company must submit an application form. The forms will be available with the brokers, underwriters, etc.

The investing public invests their saving in securities for varied reasons. They should be able to dispose the securities, in case of need. Sale of securities is a specialised activity. Hence, the companies issuing the securities, should make use of the services of agencies/institutions who are specialists in issue of securities.

Methods of new issues

The company, which raises finance through new issues, may follow any of the following methods:

a) Public issue

b) Offer for sale

c) Through intermediaries

    (i) Private placement

    (ii) Sundry intermediaries

    (iii) Managing brokers

d) Underwriting

e) Rights issue

a) Public Issues:

This is a commonly used method . It involves direct sale of securities to the public for fixed price. The company gives a notice or advertisement inviting the public to subscribe for the shares. The circular or notice or advertisement is a legal document called ‘prospectus’. No intermediaries are involved. This method is expensive.

b) Offer for sale

Under this method, shares are floated through an intermediary such as ‘Issue house’. The company allots or agrees to allot shares to ‘Issue houses’ for a fixed price. The ‘Issue house’, in turn, sells the shares to the public at a higher price. When investors buy the shares, it becomes direct allotment from the company.

c) Through intermediaries

Companies may utilise the services rendered by intermediaries for issuing shares. Intermediaries like brokers, issue houses, underwriters purchase shares from issuing companies and sell these shares to their clients.

(i) Private placement

Sometimes intermediaries may not buy the shares in their name. In selling the shares, they act as agents of the company. The shares are sold to clients. Such sales are called ‘private placement’. This method is cheaper than public issues and offer for sale.

(ii) Through sundry intermediaries

The companies may, sometimes appoint agents, salesmen, existing shareholders to secure market for their securities. But these agents or salesmen do not guarantee for the complete sale of securities.

(iii) Managing brokers

These brokers help the companies in selling the debentures or bonds. To avoid clash between competing concerns, these brokers advise the companies on matters like the right time for issue, issue terms etc. They also assist the companies in listing the securities in the stock exchanges. They help the companies to prepare prospectus, and give advertisements before the issue of shares.

d) Underwriting

Large issues are made through ‘underwriting’. Under this method the underwriters give a guarantee to the companies making new issues. They guarantee the shares offered to the public, which will be fully subscribed. In the event of less subscription, the balance of shares will be taken over by underwriters.

e) Rights issue

An existing company may get the finance required for expansion in two ways

(i) Rights issue and (ii) Issue of bonus shares.

Under rights issue method, new shares are offered to the existing shareholders. These shares are issued in proportion to the shares held by the existing shareholders. Issue of bonus shares cannot be treated as new issues.

Of all the above methods, public issues and right issue are the popular methods in India.

6.2. PROCEDURE REGARDING NEW ISSUES:

1. Issue of Prospectus

A company, which intends to raise finance from the public through new issues, must be familiar to them. The company should have gained public interest. The existing financial position and future prospects must be made known to the public. This can be done by issuing a prospectus. The prospectus is any document described or issued as a prospectus and includes any notice, circular, advertisement

or other document inviting deposits from the public, inviting offers from the public for the subscription or purchase of shares or debentures of a company.

2. Application

When a company issues the prospectus, the investors/public may apply for the shares offered by the company. These application forms may be obtained from the brokers, bankers or lead managers, who assist the company in the issue of new shares. One application is enough to apply for any number of shares. The application may be in the name of individuals or companies. The applicant usually pays an amount called ‘application money’ along with the application. It should not be less than 5 percent of the value of a share. The application money received by the company will be kept in a separate bank account opened for the purpose.

The prospectus will mention the period for which the company will receive application for shares. It is called ‘keeping the subscription list open’. Subscription list will be kept open, normally, for three days.

3. Application for listing of securities

A company can create a favourable impression in the minds of the investors about its financial soundness, marketability of its shares etc., by getting its securities listed in stock exchange. The prospectus for new issues should include details regarding submission of application form for listing of its securities in recognised stock exchanges.

4. Allotment of shares

On closing the subscription list, the company can allot shares to the applicants. After allotment of shares, the allottees become the shareholders of the company. The allotment should be made by the company only when it has received ‘minimum subscription’. This is the minimum amount required by a company to meet its fixed capital needs. It is fixed at 90 percent of the issued capital to the public. The amount should have been stated in the prospectus. Board of directors should allot the shares fairly and unconditionally. If the issue is fully subscribed, the allotment is made fully. However, if there is over subscription, the directors can allot to all applicants proportionately or to some applicants in full and reject the others. In case of over subscription, the scheme of allotment will be worked out in consultation with the stock exchange.

5. Allotment / Regret letter

After the allotment of shares, the allotment letters or share certificates be sent to the allottees within a reasonable time, say, two months from the date of closing of subscription list. Letters of regret along with refund orders must be sent to non-allotees.

SECONDARY MARKET

The secondary market refers to the market where the securities issued in the primary market are traded. The secondary market depends on the primary market. More the number of companies makes new issues in the primary market, the greater will be the volume of trade in secondary market. In India, the secondary market includes 21 regional stock exchanges, the Over The Counter Exchange of India (OTCEI) and National Stock Exchange of India (NSE).

6.3. STOCK EXCHANGE

The word **'Stock'** means a fraction of the capital of a company and the word **'Exchange'** means a place for purchasing and selling something. Stock exchanges deal in securities like shares, debentures or bonds issued by the companies or corporations in the private as well as public sector and bonds issued by the central and state governments. The Securities Contracts (Regulations) Act, 1956 defines stock exchange "as an association, organisation or body of individuals, whether incorporated or not, established for the purpose of assisting, regulating and controlling the business of buying, selling and dealing in securities".

According to Hastings " stock exchange or securities market comparises all the places where buyers and sellers of stock and bonds or their representatives, undertake transactions involving the sales of securities".

Characteristics of Stock Exchange

Following are the salient features of stock exchange

1. It is a place where securities are purchased and sold.
2. A stock exchange is a voluntary association of persons whether incorporated or not.
3. Stock exchanges do not conduct business for themselves. They provide facilities to their members to transact in company securities.
4. The trading in a stock exchange is strictly regulated. Rules and regulations are prescribed for various transactions.
5. Each stock exchange formulates its own rules and regulations. Any member who acts against the rules of the exchange can be removed from the membership.
6. Securities included in the official list of the stock exchange alone, can be traded in the stock exchange. The securities of corporations, trusts, governments, municipal corporations, companies, etc. are also dealt at stock exchanges.
7. The members of the exchange elect a governing body. It will exercise proper, direct and adequate control over the activities of the members.

8. Only members can transact in a stock exchange. Any person who has completed 18 years can become a member.
9. Both genuine investors and speculators can buy and sell shares in stock exchange.

Functions of Stock Exchange:

The functions performed by a stock exchange are as follows:

1. Ready Market: Stock exchange ensures increased liquidity and ready market for the securities. This enables it to attract people who have surplus money even for a short period of time.

2. Mobilisation of Savings: Stock exchange helps in mobilisation of surplus funds of individuals, business firms and cooperatives for investment in popular securities.

3. Evaluation of Securities: Stock exchange helps in determining the price of various securities. The prices at which transactions take place are recorded and they are made public in the form of market quotations which help the investors to know current market prices of various securities.

4. Capital Formation: Stock exchange not only mobilises the existing savings but also induces the public to save money. This facilitates capital formation in the country.

5. Proper Channalisation of Capital: Stock exchange directs the flow of savings into the most productive channels. When an existing company issues securities to raise more capital, it will be successful only if it is earning sufficient profits. Public response to such issues by weaker companies will be discouraging.

6. Fair Dealings: Stock exchanges ensure fair dealings and safety of funds because of strict regulations on the working of stock exchange. The members of the stock exchange have to operate under certain rules which checks over trading, illegitimate speculation and manipulation. Thus, stock exchange safeguards the interest of the investors.

7. Control of Corporate Sector: Every company has to conform to the rules framed by the stock exchange. Through these rules, stock exchange exercises influence on the management and working of companies in public interest

8.Barometer of Business Progress: Stock exchange acts as a barometer of the business conditions in the country. Booms and depressions are reflected by the index of prices of various securities maintained by the stock exchange.

Listing of Securities

All corporate securities like shares, stocks, bonds, debenture etc. are not allowed to be dealt with in the stock exchange. Every stock exchange maintains a list containing the names of selected companies whose securities can be traded in that stock exchange. This list is called 'official trade list' Unlisted securities cannot be dealt in the stock exchange. The company which wants its securities to be traded in a recognised stock exchange should apply to the stock exchange and get its name included in the 'official trade list'.

Meaning of Listing

The inclusion of the name of a company in the official trade list of a stock exchange is called 'listing'. Earlier, listing was optional. Listing is now made compulsory for all public companies, however, subject to certain exemptions.

Advantages of Listing

Listing gives the company a higher status. It enables a company to enjoy the confidence of the investing public. By widening the market for the securities it helps the company to raise the future finance easily. It provides price continuity for securities. It facilitates the correct evaluation of securities in terms of their real worth.

Classification of listed securities

Listed securities may be classified into two categories:

(i) Cleared Securities

(ii) Non-cleared Securities

Cleared securities are the securities in which forward trading can be done. So they are also know as "securities on forward list". Non-cleared securities are traded in spot-transactions. They are called 'securities in cash list'.

Procedure for listing of securities:

A company desirous of getting its securities listed in a stock exchange must apply in the prescribed form with the following documents and information.

1. Copies of the Memorandum and Articles of Association prospectus or statement in lieu of prospectus, director's report, balance sheet and agreement with underwriters.
2. Particulars regarding its capital structure.
3. Specimen copies of shares and debenture certificates, letter of allotment, common form of share transfer, etc.
4. A statement showing the distribution of shares.

5. In the case of existing companies, particulars of dividends and cash bonuses declared during last ten years.

6. A brief history of the company's activities since its inception.

After the scrutiny of the application, if the stock exchange is satisfied, the company should fulfill the following requirements also.

1. The company must have offered atleast 49 percent of its issued capital for public subscription through prospectus.

2. The company must be of sufficient public importance and its subscribed capital must be not less than Rs. 25 lakhs.

3. The allotment of shares to applicants should be fair and unconditional.

4. The company must execute a listing agreement. The listing agreement determines the nature of continued relationship between the company and the stock exchange.

The listing agreement should contain the following conditions and obligations to be strictly observed by the company whose securities are listed:

   a. To notify the stock exchange of the date of the Board meeting in which decision about dividend is to be taken.

   b. To notify the stock exchange, of any material change in the general nature or character of the company's business.

   c. To forward to the stock exchange copies of its annual accounts duly audited.

   d. To notify the stock exchange, of any change in the capital of the company.

   e. To notify the issue of any new shares including bonus shares.

   f. To notify the stock exchange, of any occasion which will result in the redemption, cancellation of any of the listed securities.

   g. To comply with all the requirements under the listing arrangement and not commit any breach of any condition.

5. An undertaking by the company, specifying that it shall not indulge in certain activities prohibited by law.

6. A declaration that it will abide by the rules and regulations of the stock exchange.

On complying with these conditions, the securities of the company shall be included in the official trade list.

PROCEDURE OF TRADING:

In order to buy or sell securities in a stock exchange, the following procedure has to be followed:

(i) Selection of a Broker: A non member of a stock exchange is not authorised to do any business on the floor of a stock exchange. He can transact through a broker While selecting a broker, a person can either talk directly to authorised brokers or he can act upon the advice of his friends who are already dealing with the broker.

(ii) Placing the order: Before placing an order, he can consult his friends and the broker. The order can be communicated to the broker through wire, or telephone or by meeting personally to avoid delay.

A client can place order in any of the following forms:

(a) Limit or fixed price order: Under this, the client instructs the broker to buy or sell some security at a fixed price mentioned in the order.

(b) At best or at market price order: Such an order must be executed immediately at the best possible favourable price prevailing in the market.

(c) Open order: Under this type of order, the client does not place any limit on the time during which the order is to be executed.

(d) Immediate or Cancel order : Under this type of order, the instructions of the client must be executed immediately. If the broker cannot execute the order because of unfavourable prices, it would be treated as cancelled.

(e) Stop loss order: This order is placed to safeguard against the heavy rise or fall in prices of a security. For instance, a person who has bought a share at Rs.50 and its price is going down he may place the order in the following words, “Sell at Rs.45 stop”. Thus, his loss will be restricted to Rs.5 per share.

(f) Discretionary order: A client may give a free hand to his broker to buy or sell a particular security at his discretion.

(iii) Executing the Order: After receiving the order, the broker will note it down in his diary from which it will be transferred to the ‘order book’. The broker will contact other brokers of the stock exchange and will give and receive offers to execute the order of his client. When the deal is over, the broker and the other broker with whom he has entered into the transaction will make brief notes of the price of their transactions in their diaries. After this, contract notes are prepared on the prescribed forms. A copy of the contract note is sent to the client.

(iv) Settlement: The mode of settlement depends upon the nature of the contract. It may be classified into two categories, namely, ready delivery contracts and forward delivery contracts.

Ready Delivery Contracts

A ready delivery contract involves the actual payment of the amount by the buyer in cash and the delivery of securities by the seller. A ready delivery contract is to be settled on the same day or within the period fixed by the stock exchange authorities.

Forward Delivery Contracts

Such contracts are entered into without any intention of taking and giving delivery of the securities. The traders in forward delivery securities are interested in profits out of share price movements in the future. Such transactions are settled on the settlement days fixed by stock exchange authorities.

Benefits of Stock Exchange

Stock exchange renders invaluable services to the investors and the corporations. The companies whose shares are listed and dealt in on the stock exchange enjoy better credit standing. This is because investors are aware of the fact that stock exchange exercises some element of control over the management of such companies.

Benefits to Companies

1) A company whose shares are dealt in on a stock exchange enjoys great reputation in the capital market.

2) The marketability of shares is ensured and in consequence, the company enjoys a wide market for its shares.

3) Because of their shares listed on the stock exchange, the market value of shares of a company is likely to be higher in relation to earnings, dividends and property values. This helps the company in merger plans.

4) New companies can raise funds easily from the capital market because of indirect support provided by the stock exchange.

5) The activities of speculators save the listed securities from frequent fluctuations in the prices of securities.

Benefits to Investors:

1) Stock exchange safeguards the interests of the investors. They are assured of a ready and continuous market for the securities held by them. The brokers can’t cheat the investors.

2) It provides liquidity of investments by providing a continuous market in shares and debentures.

3) Securities can be used as collateral security for loans.

4) Price quotations of stock exchange help the investor to know the real value of his investments.

5) Normally the securities of sound companies are traded in the stock exchange. The investors are saved from the risk of investment in unsound companies.

Benefits to the Community or Society:

1) The stock exchange helps in the economic development by encouraging investors to invest their savings in securities of corporate sector. It encourages capital formation in the country.

2) By encouraging marketability of securities, the stock exchange upholds the position of efficiently managed companies.

3) It facilitates a well managed enterprise to raise further funds easily.

4) It helps the Government to borrow from the public and thus enables it to undertake development projects of national importance.

5) Stock exchange helps in optimum utilisation of scarce financial resources.

6) A stock exchange is a barometer of the economic conditions of a country. It reflects the trends in the economy through fluctuation of prices of various securities.

Limitations of stock exchange:

The important limitations of stock exchange are:

1. There is lack of uniformity in organisation and control of stock exchanges.
2. There is no restriction in the membership of the stock exchanges. In India no stock exchange prescribes any minimum educational qualification for admission as a member.
3. Many times, stock exchanges have failed to control unhealthy speculation.
4. There is no proper regulation of listing of securities in the stock exchange.
5. There is no margin requirement in the stock exchange as in the case of commodity exchange.
6. More than one stock exchange is allowed to function in some cities or towns.

6.4. INVESTORS AND SPECULATORS

The main function of the stock exchange is to provide facilities to its members i.e the buyers and sellers to transact their business and to settle the transactions. The buyers and sellers are classified into two categories.

I. **Investors**

II. **Speculators**

Investors:

The investors buy the securities with a view to invest their savings in profitable income earning securities. They generally retain the securities for a considerable length of time. They are assured of a profit in cash. They are also called genuine investors.

Speculators:

The speculators buy securities with a hope to sell them at a profit, in future. They do not retain their holdings for a longer period. They buy the securities with the object of selling them and not to retain them. They are interested only in price differentials. They are not genuine investors.

Differences between Investors and Speculators

S.No	Investors	Speculators
1.	An Investor is interested in safety of his investment.	A Speculator is interested in appreciation of capital and earning profits quickly.
2.	Seeks income from his investment.	Seeks profit from sale and purchase of securities.
3.	Makes payment and takes delivery of the securities on purchasing. Receives payment and delivers the securities on sales.	He neither delivers nor takes delivery of the securities on sale or purchase.
4.	Retains holding for longer period i.e commitment is for a long term	Tries to sell the securities quickly i.e his commitment is for a short period
5.	Risk is low.	Risk is high.
6.	Stable income.	Earning of profit is uncertain.
7.	His income depends on the earnings of the enterprise.	The profit earned by him depends on the fluctuation / change in the market price of securities.

In reality, there is no pure speculator or an investor. Each investor is speculator to some extent. Similarly, every speculator is an investor, to certain extent. Hence, the difference between the two is a matter of degree only.

OPERATORS AT STOCK EXCHANGE

Members of stock exchange

a) Jobbers

Jobbers are security merchants dealing in shares, debentures as independent operators. They buy and sell securities on their own behalf and try to earn through price changes. Jobbers cannot deal on behalf of public and are barred from taking commission. In India, they are called Taravaniwalas.

b) Brokers

Brokers are commission agents, who act as intermediaries between buyers and sellers of securities. They do not purchase or sell securities on their behalf. They bring together the buyers and sellers and help them in making a deal. Brokers charge a commission from both the parties for their service. Brokers are experts in estimating trends of price and can effectively advice their clients in getting a fruitful gain. Brokers get orders from investing public and execute the orders through Jobbers and they are entitled to a prescribed sale of brokerage.

Non-members acting for members:

Some non-members with limited rights are allowed to enter the house and to act on behalf of members. There are two types of such agents.

a. Remiser

He acts as an agent of a member of a stock exchange. He obtains business for his principal ie., the member and gets a commission for that service.

b. Authorised clerk

The authorised clerks are mere employees of the members, appointed by the member of stock exchange. The authorised clerks transact business on behalf of their employers on the floor of the stock exchange. They are paid a salary, plus a commission.

SPECULATION

Speculation refers to the buying and selling of securities in the hope of making a profit from expected change in the price of securities. Those who engage in such activity are known as ‘speculators’.

A speculator may buy securities in expectation of rise in price. If his expectation comes true, he sells the securities for a higher price and makes a profit. Similarly a speculator may expect a price to fall and sell securities at the current high price to buy again when prices decline. He will make a profit if prices decline as expected.

The benefits of speculation are: (i) It leads to smooth change and prevents wide fluctuations in security prices at different times and places. (ii) Speculative activity and the resulting effect in the prices of securities provided a guidance to the public about the market situation.

Speculation and Gambling

Speculation and Gambling operations may appear to be the same. In both cases, the profit or losses depend upon future events, which are uncertain. The objective in either case is to make quick profits. However there are certain differences between them.

S.No	Speculation	Gambling
1.	It is based on knowledge and foresight.	It is based on chance of events happening.
2.	It is a lawful activity.	It is an illegal activity.
3.	It performs economic functions.	It has no benefits to offer to the economy.
4.	Speculators bear the risk of loss on the basis of logical reasoning.	Gamblers bear the risk of loss on the basis of blind and reckless expectation.

KINDS OF SPECULATORS

There are four types of speculators who are active on the stock exchanges in India. They are known as Bull, Bear, Stag, and Lame Duck. These names have been derived from the animal world to bring out the nature and working of speculators.

Bull

A Bull or Tejiwala is an operator who expects a rise in prices of securities in the future. In anticipation of price rise he makes purchases of shares at present and other securities with the intention to sell at higher prices in future. He is called bull because just like a bull tends to throw his victim up in the air, the bull speculator stimulates the price to rise. He is an optimistic speculator.

Bear

A bear or Mandiwala speculator expects prices to fall in future and sells securities at present with a view to purchase them at lower prices in future. A bear doesnot have securities at present but sells them at higher prices in anticipation that he will supply them by purchasing at lower prices in future. A bear usually presses its victim down to ground. Similarly the bear speculator tends to force down the prices of securities. A bear is a pessimistic speculator.

Stag

A stag is a cautious speculator in the stock exchange. He applies for shares in new companies and expects to sell them at a premium, if he gets an allotment. He selects those companies whose shares are in more demand and are likely to carry a premium. He sells the shares before being called to pay the allotment money. He is also called a premium hunter.

Lame Duck

When a bear finds it difficult to fulfill his commitment, he is said to be struggling like a lame duck. A bear speculator contracts to sell securities at a later date. On the appointed time he is not able to get the securities as the holders are not willing to part with them. In such situations he feels concerned. Moreover, the buyer is not willing to carry over the transactions.

6.5. SECURITIES AND EXCHANGE BOARD OF INDIA (SEBI)

For proper development of Indian stock market, the functioning of stock exchanges must be brought under the control and supervision of an independent regulatory agency. Central government, therefore established SEBI.

SEBI

The SEBI was set up as an administrative body in April 1988. It was given statutory status on 30.1.92 by promulgation of SEBI ordinance. The ordinance is considered to be an Act of parliament.

Objectives:

1. The basic purpose of establishing SEBI is to protect the interest of the investors in securities.
2. To promote, develop and regulate the securities market and deal with the matters connected therewith or incidental thereto.

When SEBI was established as a board in 1992, the task before it was to regulate the functions and conduct of intermediaries in the stock market, check insider trading and ensure fair play in takeover bids by a code of conduct.

Features of SEBI

1. The SEBI shall be a body corporate established under SEBI ACT, with perpetual succession and a common seal.
2. The head office of the board shall be at Mumbai. SEBI can have branch offices at other places in India.
3. The board shall consist of the following members.

(i) A chairman

(ii) Two members from amongst the officials of the Ministries of the Central Government dealing with finance and law.

(iii) One member from amongst the officials of the Reserve Bank of India.

(iv) Two other members

Chairman and other members of the Board are appointed by the central Government.

4. The general superintendence, direction and management of the SEBI shall vest in the Board of members. Those members exercise all powers and do all acts and things which may be exercised by the Board (SEBI)
5. Central Government shall have the power to remove a member or the chairman appointed to the Board
6. Central government shall provide finance and also make appropriate grants to the Board.
7. Central government has power to issue direction to the board on the policy matters and shall supercede the board in the event of default by the Board.

Functions

To provide the development of, and to regulate the securities market SEBI undertakes the following function

1. Regulating the business in stock exchanges.
2. Registering and regulating the working of stock brokers, sub- brokers, issue bankers, underwriters and such other intermediaries who may be associated with securities markets in any manner.
3. Registering and regulating the working of collective investment schemes including mutual funds.
4. Promoting and regulating self-regulatory organisations.
5. Prohibiting fraudulent and unfair trade practice relating to securities market.
6. Promoting investor’s education and training of intermediaries of securities market.
7. Prohibiting insider trading in securities.
8. Regulating substantial acquisition of shares and take-over of companies
9. Calling for information from, undertaking inspection, conducting inquires and audits of the stock exchanges
10. Performing such functions as may be delegated to it by the central government.

ROLE OF "SEBI" IN A STOCK EXCHANGE

The Securities and Exchange Board of India (SEBI) Act, 1992 was passed by Central Government for establishing a board to protect the interest of investors in securities and to promote the development of and to regulate the securities market and for matters connected therewith or incidental thereto.

Every stock exchange needs recognition from Central Government. SEBI helps the Government in ensuring compliance of rules for recognition . Any stock exchange, which is desirous of being recognized, may make an application to the Central Government. The application should be accompanied by a copy of the bye-laws of the stock exchange for the regulation and control of contracts and a copy of the rules relating, in general, to the constitution of the stock exchange. The application forms received are scrutinized by SEBI. Recognition may be given to a stock exchange subject to the fulfillment of the following conditions:

a) Bye laws of the exchange should ensure fair dealings and it must protect the interests of investors and the trade

b) Compliance of other conditions imposed by the Central Government.

SEBI's powers in relation to stock exchanges

The SEBI ordinance has given it the following powers:

(i) It may call periodical returns from stock exchanges.

(ii) It has the power to prescribe maintenance of certain documents by the stock exchanges.

(iii) SEBI may call upon the exchange or any member to furnish explanation or information relating to the affairs of the stock exchange or any members.

(iv) It has the power to approve bye-law of the stock exchange for

regulation and control of the contracts.

(v) It can amend bye-laws of stock exchange.

(vi) In certain areas it can grant to licence the dealers in securities.

(vii) It can compel a public company to list its shares.

Securities Contract (Regulation) Act empowers Central Government to delegate some of its powers, to SEBI. They are as follows:

1. Power to grant recognition to a stock exchange.
2. Power to direct any stock exchange to amend the rules relating to constitution of stock exchange, admission of new members, etc.
3. Power to supersede governing body of any stock exchange.

4. Power to suspend business of a recognised stock exchange.
5. Power to prohibit contracts in certain cases.

Working of SEBI

SEBI has been carrying on its duties successfully. It has issued and clarified guidelines on disclosure and investor protection. It has also issued guideline for merchant bankers, advertising code for mutual funds.

To safeguard the interests of investors, it has registered a number of investors associations. A series of advertisement are also being issued by SEBI to educate investors. Also, it has recognised many self-regulatory organisations.

OTC EXCHANGE OF INDIA

OTCEI (Over the Counter Exchange) was set up to address the problems of both investors and small and medium sized companies whose shares could not be listed on any stock exchange. OTECI was promoted by premier financial institutions such as UTI, ICICI, IDBI, SBI, IFCI, GIC and Canbank Financial Services. It is a recoginised stock exchange under sec 4 of Security Contract (Regulation) Act.

6.6. MUTUAL FUNDS: DEFINITION

The Securities and Exchange Board of India (Mutual Funds) Regulations, 1993 defines a mutual fund as "a fund established in the form of a trust by a sponsor, to raise monies by the trustees through the sale of units to the public, under one or more schemes for investing in securities in accordance with these regulations."

Mutual funds collect the savings from small investors, invest them in government and other corporate securities and earn income through interests and dividends besides capital gains. It works on the principle of 'small drops of water make a big ocean'

To get funds from investors, the fund adopts a simple technique. Each fund is divided into a small fraction called 'units' of equal value. Each investor is allotted units in proportion to the size of his investment.

ADVANTAGES

1. Mutual funds mobilise the savings of small investors and direct them towards capital investment of corporate bodies.
2. Small and medium investors can enjoy wide portfolio of investment held by the mutual fund. The fund diversifies its risks by investing on a large variety of shares and bonds, which cannot be done by small and medium investors.

3. They provide better yield to their customers. Mutual funds enjoy economies of large scale. The profits earned by them are passed to the investors by way of dividends and capital appreciation.
4. They render expertised investment service at low cost.
5. Certain funds exclusively offer tax benefits to its customers.
6. Some Mutual funds permit the investors to exchange their units from one scheme to another. Thus, they provide flexible investment schedule.
7. Provides greater liquidity and affordability to small investors, ie., investors can sell units to the funds at any time. In the absence of MFs, small investors cannot think of participating in investment on share capital of large companies.
8. Mutual funds play a vital role in the development of capital markets by providing a sustainable domestic source of demand for securities.
9. Promotes industrial development by mobilising the savings of small investments and supply fixed capital of industrial undertakings.
10. Act as substitute for initial public offerings (IPO's).

Thus mutual funds provide stability to share prices, safety to investors and resources to entrepreneurs.

6.7. BOMBAY ONLINE TRADING SYSTEM (BOLT)

BOLT is the online trading system in use at the stock exchange, Mumbai since March 1995. It is one of the few stock trading systems in the world that handles hybrid/mixed models of trading; both order-driven and quote-driven. It supports the normal segment and continuous net settlement. There are now 6000 Bombay Stock Exchange (BSE) trading terminals spread across the country.

BOLT: How does it work?

Brokers send their quotes, orders, negotiated deals and in-house deals from their offices to the Central Trading Engine (CTE) from their broker's workstation. The best bid and the best offer is available to all broker workstation using a mechanism called "Broadcast of market information". The buy and sell orders placed by the brokers/traders are matched with the best available price in market for that security (Scrip). After they are matched and the transaction concluded, a conformation is sent to the broker, which can be printed out.

Strength of BOLT

1. Reduces or eliminates operational inefficiencies inherent in manual systems.
2. Increases the trading capacity of the stock exchange.

3. Improves transparency, eliminates unmatched trades.
4. No delay in reporting.
5. Smooth market operations using the latest technology.
6. Provides trade using electronic media to the broker using an interface with the broker's back-office systems.
7. Provides user information like scrip prices and indices
8. Provides analytical data to the stock exchange.
9. For better control of stock exchange operations BOLT allows setting of various checks limits.

Achievement of the BOLT

The achievements of the BOLT system are:

1. An average response time of less than two seconds.
2. On an average 3.4 million market queries are handled daily.
3. The system can support more than 10,000 users.

Points to Remember

Primary market denotes the market for new issues of Shares and Debentures.

❖ **Methods of new-issue**

1. Public issue 2. Offer for sale 3. Through intermediaries 4. Underwriting 5. Rights issue 6. procedures regarding new issue a. Issue of prospectus b. Application c. Application for listing of securities d. Allotment of Shares The Stock Exchange in an organised second hand market for purchase and sales of corporate securities.

❖ **Functions of Stock Exchange**

1. Ready Market 2. Mobilisation of Savings 3. Evaluation of Securities 4. Capital formation 5. Proper channalisation of Capital 6. Fair Dealings 7. Control of corporate sector 8.Barometer of Business progress

❖ **Listing of securities**

It means the inclusion of securities in the official list of a stock exchange.

❖ **Procedure of trading**

1. Selection of a Broker 2. Placing the order 3. Executing the order 4.Settlement

❖ **Benefits of stock exchange**

1. Benefits to companies   2.Benefits to investors

3. Benefits to community

❖ **Operators at Stock Exchange**

a. Jobbers   b. Brokers

❖ **Kinds of speculators**

a. Bull   b. Bear   c. Stag   d.Lameduck

The SEBI Act, 1992 provided the establishment of a statutory Board with 6 members

QUESTIONS

I. Objective Type:

I. Choose the correct answer:

1. The first issues are floated in

   a) Primary market   b) Secondary market

   c) Commodity marketd) Regulated market

2. The popular method of sale of new shares in India is

   a) Public issue   b) Offer for sale

   c) Managing brokers d) Underwriting

3. Stock exchanges deal in

   a) Goods   b) Services

   c) Financial securities   d) Country's currency

4. Number of recognised stock exchange in India

   a) 2   b) 21   c) 22   d) 24

5. Stock exchange allow trading in

   a) All types of shares of any company

   b) Bonds issued by the Government

   c) Listed securities

   d) Unlisted securities

6. Jobbers transact in a stock exchange

   a) For their clients   b) For their own transactions

   c) For other brokers   d) For other members

7. A pessimistic speculator is

   a) Stag   b) Bear   c) Bull   d) Lame duck

8. An optimistic speculator is

   a) Bull   b) Bear   c) Stag   d) Lame duck

9. Securities Contract Regulation Act was passed in

   a) 1952   b) 1956   c)1964   d) 1966

10. SEBI is formed as per

    a) Securities contract (Regulation) Act

    b) Securities and Exchange Board of India Act

    c) Companies Act

    d) Indian constitution

11. A bull operator believes in

    a) Increase in prices   b) Decrease in prices

    c) Stability in prices   d) No change in prices

12. Stock exchange …………… speculation in shares

    a) Does not allow   b) discourage   c) encourage   d) prohibits

13. A cautious speculator is known as

    a) Stag   b) Bull   c) Lame duck   d) Bear

14. A stock exchange is a place to

    a) Exchange one security for another

    b) Buy and sell financial securities

    c) Float new shares

    d) Buy and sell stock of goods.

15. SEBI has the following number of members including chairman.

    a) 5   b) 7   c) 6   d) 8

Ans : 1.a, 2.a, 3.c, 4.b, 5.c, 6.b, 7.b, 8.a, 9.b, 10.b, 11.a, 12.c, 13.a, 14.b, 15.c.

II. Fill in the blanks:

1. Large scale undertakings are organised in the form of ______________ .
2. Joint stock companies require ___________________________
3. The long term capital required by the company is divided into small units of fixed amount called ___________
4. Shares represent ___________________ interest.
5. Debentures denote __________________ interest.
6. _______________ is an acknowledgement for raising loan from the public.
7. Primary market is concerned with ________________
8. Secondary market deals with ___________ traded in primary market.
9. Companies are assisted by _____________ to make new issues.
10. ________________ is a commonly used method of issuing shares.
11. ______________________ act as intermediary to float new shares.
12. __________ is an invitation to the public to subscribe for the shares.
13. After allotment of shares, allottees become the _____________ of the company.
14. Application money should not be less than ____ percent of the value of a share.
15. Minimum subscription is fixed at ___________ of the issued capital.
16. The volume of business in secondary market depends on _______________
17. Secondhand securities are traded in __________________________________
18. There are __________________ regional stock exchanges in India.
19. Inclusion of securities in the official list of stock exchange is called ___________
20. Listing is _____________________ for public companies.
21. Cleared securities are also called ____
22. _____________ order gives a freehand to the brokers of a client to buy or sell a particular security for any price.
23. Ready delivery contracts are also called as _____________________
24. Investors retain securities for ________________________ period.
25. _____________________ are the employees of the members of a stock exchange.

26. Stag is called ___________________

27. _________ is the supervisory body established to regulate Indian stock market.

28. _____________ enables small investors to participate in the investment on share capital of large companies.

29. ______________ act as a substitute for initial public offering.

30. BOLT is the online trading system in use at _______________ stock exchange.

Ans:

1. Joint stock companies.	2. Enormous capital.
3. Shares.	4. Ownership.
5. Creditorship.	6. Debentures.
7. Issues of new shares.	8. Resale of securities.
9. Brokers/under writers.	10. Public issue.
11. Issues Houses .	12. Prospectus.
13. Shareholder/member.	14. 5.
15. 90%.	16. Primary market.
17. Secondary market	18. 21.
19. Listing.	20. Compulsory.
21. Securities on forward list.	22. Discretionary order.
23. Spot Contracts.	24. Longer.
25. Authorised clerks.	26. Premium hunter.
27. SEBI	28. Mutual funds.
29. Mutual funds.	30. Mumbai.

III. Match the following:

1. Primary market	a) Tejiwala
2. Secondary market	b) Mandiwala
3. SEBI	c) Tarawaniwala
4. Bull	d) New issues market
5. Bear	e) Supervisory Body
	f) Resale of securities.

Ans: 1. d, 2. f, 3. e, 4. a, 5. b.

IV. Short Questions:

1. What is a security?
2. How can we classify securities market?
3. What do you mean by public issues?
4. What is 'private placement'?
5. What is ' underwriting'?
6. What is prospectus?
7. What is share application?
8. What is share allotment?
9. What is minimum subscription?
10. What is a secondary market?
11. Define a stock exchange
12. What is listing?
13. What are the advantages of listing?
14. Classify the listed securities
15. What do you mean by ready delivery contracts?
16. What are forward delivery contracts?
17. What are the limitations of stock exchange?
18. Who is a speculator?
19. Who is an investor?
20. What is speculation?
21. What is the difference between speculation and Gambling?
22. Who is a jobber?
23. Who is a broker?
24. Which non-members can act in stock exchange?
25. Who is called a 'Lame duck'?
26. What is SEBI?
27. What is OTCEI?

28. Define mutual funds

29. What is BOLT?

30. What are the achievements of BOLT?

V. Answer in about a page:

1. Describe securities market.
2. What are the methods of new issue of shares ?
3. Explain the procedure for listing of securities.
4. Differentiate between Investors and speculators.
5. Who are the operators at a stock exchange ?
6. Explain the different kinds of speculators.
7. Explain how BOLT works, and the strengths of BOLT.

VI. Essay type:

1. How are new issues floated in the primary market. Also explain the procedure for the new issues?
2. Define Stock Exchange. Explain its characteristics and functions.
3. Describe the procedure for trading in a stock exchange.
4. What are the benefits and limitation of a stock exchange ?
5. Explain the objectives, features, functions and powers of SEBI.

CHAPTER - 7
CO-OPERATIVES

" ALL FOR ONE AND ONE FOR ALL "

- DUMAS

Learning Objectives : After reading this chapter you will be able to learn the following.

- ❖ 7.1. Definition – Special features of Co-operatives.
- ❖ 7.2. Merits and demerits of co-operatives.
- ❖ 7.3. Type of Co-operatives
  - ❖ Co-operative Credit Society.
  - ❖ Co-operative Super Market.
- ❖ 7.4. Differences between Companies and Co-operatives.

INTRODUCTION

In the previous chapters we have studied sole trading business, partnership and joint-stock companies. All these forms of business organisation are profit oriented. The shares are in their control. Their profit is distributed in the ratio of capital invested. Co-operative society is just the opposite of these in which members, inorder to achieve a common economic objective, voluntarily work together. Co-operation is a mid-way between capitalism and communism.

There are many economically weaker sections in the society. Among them are, farmers, craftsmen and small traders. These ill- fated people are crushed under the clutches of the mediators and money lenders. Their main aim is to earn profits. For instance, the farmers are unable to sell their produce at remunerative prices. They also buy the agricultural inputs at an unreasonable prices. They are facing hardships from middlemen and brokers. In these circumstances co-operative

enterprises emerged as an instrument to protect the interest of the weaker sections. The philosophy behind the concept is “ All for each and each for all”.

The word co-operation is derived from the Latin word “Co- operari” meaning “ to work with”. So co-operation means working together with others for a common purpose.

HISTORY

The co-operative movement can be traced back to about 150 years. ROBERT OWEN started the first ever co-operative movement in the year 1844 with 28 members called as ROCH DALE society of Equitable pioneers. It was a consumer’s co- operative society. The father of this movement was ROBERT OWEN.

In India, the poverty and rural indebtedness were predominant during the 19th century. As a fuel to the fire, a great famine occurred in 1901. In order to find a solution to these problems, the government brought out a statute known as Co-operative Societies Act 1904. But the scope of this Act was restricted to the credit facility only. A comprehensive Act was brought again in the year 1912 covering the formation, management and regulation of the co-operative societies.

In 1914, a committee headed by Meclagaon, was appointed by the government to review the working of co-operatives. On the basis of this recommendation of the committee the governance of co-operatives was transferred from the central to the state governments. At present, the state governments are monitoring these institutions under a separate ministry.

7.1. DEFINITION

The co-operative society is yet another form of business organization. It is formed in a similar manner like a joint stock company. It is a unique form of organisation. It is started with the motive of organising and rendering services to its members. The definitions provided by different authors and leaders of the movements are given below.

1. According to H.C. Calvert “ A co-operative society is a form of organisation wherein persons voluntarily associate together as human beings on the basis of equality for the promotion of economic interests of themselves”.

2. According to Sir Horace Plunkett “ Co-operation is self-help rendered effective by organisation. It is better farming, better business, better living”.

3. According to Talmaki “ It is an association of the weak who gather together for a common economic need and try to lift themselves from weakness into strength through business organisation.

4. The Indian Co-operative Societies Act, 1912 defines a co- operative enterprise

as, “A society which has its objectives for promotion of the interests of its members in accordance with the principles of co-operation”.

5. Prof. Lambert defines a co-operative society as “An enterprise formed and directed by an association of users, applying within itself, the rules of democracy and directly intended to serve both its own members and the community as a whole”.

Principles of Co-operation

A co-operative enterprise works on the basis of the following principles to protect the interests of its members. The features of a co-operative society can be studied as under

1. Voluntary Organisation

A co-operative society is a voluntary association of persons. Any person can join the society . There is no compulsion to become a member of a co-operative society . A person can join a co-operative society whenever he likes and leaves it when ever he wants.

2. Equality

In a co-operative society all persons are equal. Its members have equal rights and more capital does not provide more rights to an individual.

3. Democratic Managements

Co-operative societies are managed on democratic lines. Every member has only one vote irrespective of the number of shares held by him. The society is formed on the principle of democracy which means “ One vote for one member”. A General body meting is conducted annually. Representatives are elected by the members to manage the society.

4. Combination of resources

In this organisation members pool their own resources. They use their resources in the interest of all members.

5. Concentrated Effort

In this organisation all individuals work together. The main principle of co-operation is that “ Each for all and all for each “.

6. Spirit of service

The objective of co-operative organisation is that the service is primary and profit is secondary. It strives to provide required services to the members. Provision of credit facility, construction of buildings, supply of seeds, fertilizers etc., are some

of the services offered by the societies.

7. Plural Membership

It is an association of persons. A minimum of 25 persons are required to form a co-operative society. There is no limit on the maximum membership.

8. Legal Capacity

An individual must have the legal capacity to make any agreement. They are bound by the rules and regulations of the society. The members forming the co-operative society must have attained the age of majority.

9. Open Membership

Any man or woman having a common interest can join a society at any time. No discrimination is made on the basis of caste, creed or religion. Both the rich and the poor can join. Illiteracy is also not a bar to membership.

10. Finance

The capital of co-operative society is divided into many shares of equal value. The society also gets capital from its members. But the share value is fixed at low. A person becomes a member by purchasing its shares.

11. Limited return on Capital

A co-operative society gives less importance to money power. A minimum of 9 % of the profits is to be distributed as dividends. This prevents rich people from dominating the society.

12. Local Membership

Generally, in any co-operative society people from the particular locality become members. This is because only people in a particular locality can have a common economic problem. They are also well known to each other.

13. No Political Influence

A politician can join a co-operative society as a member, but politics should not enter into its management. This makes a co- operative society, non – political.

14. State Control

Though the co-operatives are voluntary enterprises, the Government exercises control and supervision over their functioning. They have to observe all the rules framed by the Government. Every society has to submit to the Government, its annual statements and audited accounts. The details of deposits and loans are to be reported regularly.

15. Distribution of Surplus

The Profit of co-operative societies is distributed to the members in Proportion of purchases made by them and not on shares held by them. According to the Co-operative Societies Act of 1983 Section 72(1) (a) the disposal of net profits has been mentioned. The payment of dividend on shares to members will be at the rate of 14% per annum on the paid up value of shares. The surplus of the profit is used to give bonus to members or rebate on the sales effected by them. This is known as "Distribution Surplus"

16. Registration

Registration is compulsory for all the societies. Every society should be registered as per the provisions of the Co-operative societies Act of 1912 or any Act passed by the state Government. An unregistered society cannot use the word “co-operative” in its name.

17. Separate legal entity

A co-operative society becomes a separate legal body after its registration. It can own property and make contracts in its own name. It can also sue and be sued in its own name.

18. Liability

The liability of the members of a co-operative society is generally limited to the capital taken by them. But in a village society, the members liability can be unlimited.

19. Mutual Help

The main principle of co-operative organisation is the mutual help. Every member of the society is expected to help himself and also help every other member.

20. Statutory Audit

The Government inspects the activities and the accounts through co-operative audit department.

21. Cash Trading

Credit transactions are not permitted in the societies. The entire trading is carried on cash basis. All the receipts and payments are made in terms of cash. As such, it eliminates bad debts.

22. No share transfer

A co-operative society is formed by persons who join on their own. A person can join or leave the society whenever he wishes. But a member cannot transfer his membership to another. But it will repay the share capital to an outgoing member.

23. No Speculation

The list of shares of a co-operative undertaking is always open to new members. Moreover, the shares are sold at par value. Therefore, a co-operative society is free from speculation on its shares.

24. Corporate Status

When a co-operative society is registered it becomes a body corporate. It has separate legal existence. It has perpetual succession and common seal.

25. Training in Co-operation

The success of co-operative enterprise depends upon the awareness of its members. Training is provided to the members to educate them about the objectives of the society.

7.2. MERITS

A number of advantages are derived from the system of co- operative societies. They are given below.

1. Easy formation

It is easy and less costly to form a co-operative society. Procedure for registration is very simple.

2. Unlimited membership

There is no restriction in respect of maximum number of members. Every person is at liberty either to enter or to leave the organisation as and when he likes.

3. Democratic management

Management of a co-operative society is fully democratic. Every member has an equal vote irrespective of his capital contribution. The principle of 'one man one vote' is followed. There will be no domination by any group of persons.

4. Limited liability

The liability of the members of the society is restricted to the extent of their share capital. So the private properties of the members cannot be touched in discharging the liabilities of the firm.

5. Stability

After registration, a co-operative society becomes a separate legal entity. The death, lunacy, or insolvency of a member does not affect its existence. It enjoys continuity of operations.

6. Economy in management

Generally, the members themselves manage a co-operative society. The members of the managing committee offer honorary services to the society. The publicity expenses are minimised.

7. Cheaper service

It offers better service at cheaper costs. Service is the primary objective, while profit is secondary.

8. Tax concession

Income tax is not levied on the income of the co-operative enterprises. It is exempted from payment of income tax, stamp duty, registration fee etc.,

9. Social benefit

Co-operatives are non-competitive organizations. They promote personal liberty, social justice and mutual co-operation.

10. Saving habit

It promotes saving habit, self-help and other moral values in the society.

11. State patronage

The objective of the government is to uplift the socially and economically backward groups. To achieve this objective, liberal financial assistance is arranged to the weaker sections. The patronage of the state is a boon to the co-operatives.

12. Eleminating middlemen

There are a number of traders between the producer and the consumer. Each one in the chain makes profit. A co-operative society reduces the difference between the producer's price and the consumer's price.

13. Fall in prices

The essential goods are supplied to the members at cheaper rates. Due to its impact, the price level in the market will come down.

14. Employment

Trade and industry have flourished in the co-operative sector with the aid of the state. They create employment avenues in the market. For example, the government has established several sugar and spinning mills and provided jobs to the people.

15. Government help

Co-operatives are fully nurtured with the Government patronage from the time of its inception. In India co-operatives are actively sponsored and supported by the state.

7.2. DEMERITS

In spite of the above advantages, the growth of co-operative societies is not satisfactory and encouraging. The reason is that it suffers from certain weakness and limitations. The following are the demerits of a co-operative society.

1. Inefficient management

Members of a co-operative society do not generally possess the ability and experience to manage the business efficiently. They do not take proper interest in the management. It cannot afford to employ persons with necessary ability, knowledge and experience.

2. Limited capital

A co-operative society is formed usually by people with limited means. The principle of 'one man one vote' discourages the members to invest large amount. Therefore co-operative society often faces shortage of funds. It is not able to mobilise adequate capital for large scale operation.

3. Lack of motivation

Absence of profit motive and minimum 9% rate of dividend suppress the zeal and responsibility on the part of the management. The employees also do not have interest to work hard as they get low salaries.

4. Lack of co-operation

Sometimes the members may not have unity among themselves. It might affect the business of co-operatives.

5. Domination of vested members

Some members try to command society by virtue of their managerial interest and political power. They exploit the society as their own property.

6. Non-transferability of interest

The shares of a co-operative society are not transferable. A member who wants to quit the society has to surrender his shares to the society to get his money back.

7. Lack of secrecy

The business affairs of a co-operative society are openly discussed in the meetings. Every member is free to inspect the books and records of the society. Therefore, it becomes difficult to keep the secrets of business.

8. Excessive government control

The day to day working of a co-operative society is bound by legal rules and regulations. Reports have to be submitted to the Registrar of co-operative societies Time-consuming formalities restrict flexibility and initiative.

9. No credit facility

Since credit facilities are not usually offered to members, they may not be interested in buying goods for cash.

10. Political rivalries

Directors or members of the executive committee are not generally elected on the basis of their skill knowledge, experience and honesty. But they are elected on the basis of caste, political connections and groups. They are mainly responsible for the failure of many co-operative societies.

Formation of a co-operative society

A co-operative society must be registered under the Co- operative Societies Act, 1912 or any other state Co-operative law.

A co-operative society can be started with a minimum of 25 persons, having a common interest.

An application has to be submitted to the Registrar of Co- operative Societies expressing their intention.

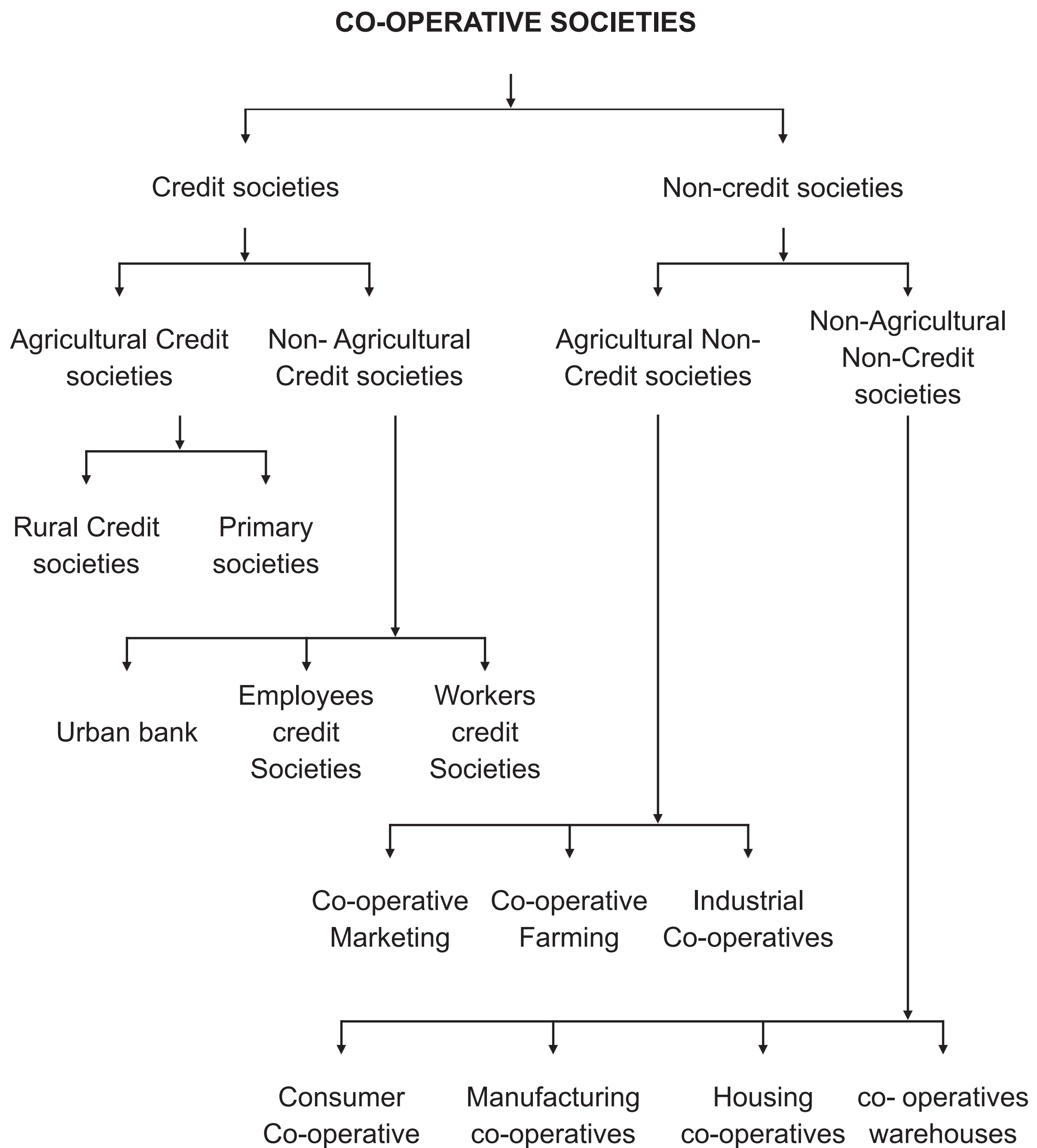
The application form is known as Memorandum of Association.

It should contain the name and address of the society its objectives, the capital and liability of the members.

A copy of the bye-laws stating the rules and regulations of the society should be attached along with the application form.

The system of management, procedure with regard to meetings, resolutions, are stated in the bye-laws. The Registrar will, carefully scrutinise the documents in order to ensure that they are in accordance with the provisions of the Act. When he is fully satisfied he will enter the name of the society in his register and issue the Certificate of Registration. By issue of this certificate, the society comes into existence as a body corporate having a separate legal entity.

Chart showing the types of co-operatives



7.3 TYPES OF CO-OPERATIVES

The area of co-operation is very extensive. Actually wherever there are middlemen and there is a chance of securing advantages by exploitation, the movement of co-operation came into play. Subsequently, various forms of co-operation are in existence. Some chief forms are as follows:

7.3.a. Credit societies

They are voluntary association of people with moderate means. They are formed with the object of giving short-term finance to members. In this way, the co-operative society protects its members from the clutches of the moneylenders. They can be classified in to two types.

A. Agricultural credit societies

It is the credit society, organised mostly by agriculturists of a village. They provide loans to its members for various productive and unproductive purposes relating to Agriculture. Agriculture credit societies are also called as rural credit societies or primary societies.

Rural credit Societies

It is located in rural areas. It secures funds by way of selling shares and by accepting deposits from members and non-members. They lend for productive purpose to small farmers and marginal farmers. They are formed at villages. Its aim is to help their members in developing the habit of savings and banking habit. They also help in collecting rural savings for national development. The liability of the members is unlimited.

B. Non-Agricultural credit society

Non-agricultural credit societies are formed by the people living in towns and cities. Their aim is to provide loans to members for productive purposes. These may be classified in to three types.

1. Urban Banks

These banks are located in urban areas. Therefore these societies are called urban credit societies. The liability of the members is limited. They receive deposits from members as well as non-members. These funds are used to grant loans to the members at low rate of interest. They do the banking business as that of the commercial banks.

2. Employees credit societies

It is formed by persons with limited means. It aims to provide financial assistance to its members. They promote the habit of saving and thrift among the members. The employees of a business organisation form a society to get credit facilities on long term basis at a reasonable rate of interest.

3. Workers credit societies

These credit societies are formed by unskilled and semi- skilled labourers of an organisation. The intention is providing short- term finance to members on an

auction basis. The loan amount has to be recovered on an equated monthly basis along with interest thereon.

C. Non-credit societies

These societies are considered to be a solution for many economic problems. They are formed in different areas of economic life of men. These may be grouped under two categories, which are as follows.

a) Agricultural Non-credit societies

b) Non-agricultural Non-credit societies

a. Agricultural Non-credit societies

These societies have helped members of limited means to secure loans at low rate of interest. They are assisting the members in marketing, farming and industrial services. The following are its types.

(i) Co-operative marketing societies

Marketing co-operatives help the members to secure fair price for their products. They may purchase the produce from the members and sell in bulk when the market is favourable. In some cases co-operatives sell the produce of the members on commission basis. Marketing co-operatives advance loans to the members. These societies eliminate middlemen and help the members to secure better price for their product.

(ii) Co-operative farming societies

These societies are organised by landowners and agriculturists. The main aim is to secure the advantage of large scale farming and produce maximum produce with the lowest cost. These societies would solve the problems of agriculture like poor yield.

(iii) Industrial co-operatives

An industrial co-operative is organised by small scale producers. Co-operative undertakings are a useful means of developing small scale and cottage industries. Industrial co- operatives are very useful in obtaining raw materials, in improving the quality of products.

b. Non-Agricultural Non-credit societies

They are formed in order to assist the middle and lower income groups of people. Their main aim is for rendering different types of service to their members at nominal rates of interest. The different types are

1. Consumer’s co-operatives 2. Manufacturer’s co-operatives

3. Housing co-operatives and 4. Co-operative warehouses.

1. Consumer’s Co-operatives

A co-operative society organized by consumers of a locality for supplying essential goods at a reasonable price. This is called a consumer co-operative society. It eliminates the middlemen. They purchase their requirements directly from the producers or wholesalers in bulk and sell to members, non-members at a reasonable price.

2. Manufacturer’s co-operatives

These societies are mainly formed in urban areas by the manufacturers belonging to the same industry. They help their members in getting essential raw materials, government grants, tax subsidies, labour forces and other essential requirements. Brick manufacturers co-operative societies, textile mill owners co-operative societies are the few examples.

3. Housing co-operatives

Every person likes to have his own house. So people who would like to have own houses and do not have sufficient money may start a co-operative house building society. These societies will advance loans to members for the construction of houses. The loan amount is to be repaid in easy installments.

4. Co-operative warehouses

These are mostly found in rural areas. It helps the members to get the facility of storing agricultural inputs. They will keep the finished goods, till they are despatched for sale through marketing co-operatives.

7.3.b. Co-operative super markets

This term is basically an Indian one, but it is derived from English expression “ super market”. It refers to a type of large scale retailing. The articles of daily use are sold in different departments without the help of sales persons. It is usually started as a joint stock company to earn profit. They are usually located only in cities and big towns. They must have large daily turnover to earn profit on their large capital outlay. In India the first supermarket was started in New Delhi.

Super markets have a dominant provision section, with more varieties. Other sections relating to clothing, footwear, stationery, crockery and other house hold items are displayed with their prices. The prices are fixed. There is no bargaining. Door delivery of goods is also given. Sales are made only for cash. Now a days credit cards are also accepted.

M.M.Zimmerman defined super market as “ A departmentalized retail establishment having four basic departments i.e., self-service grocery, meat and dairy products, plus other house hold departments, and doing a maximum business. It may lease departments on a concession basis”.

Features

1. It is a form of large scale retailing.
2. There is a wide variety of goods made available.
3. The system of self-service is used.
4. There is no need for sales men in self services section.
5. The layout is in the form of different departments.
6. Sales are on cash basis.
7. Goods are sold after cleaning and packing.
8. No adulteration is practiced.
9. Correct weighments are used, so that consumers are not cheated by short weighing.
10. Scarce commodities are also supplied.

Merits

1. Customers are able to buy the goods of daily use at one place.
2. The profit of the super market is shared with the customers in the form of low price of products.
3. They can move around the stores and buy in a relaxed manner and choose the articles they like.
4. Super markets are able to attract many customers and thereby register more turn over.
5. The commodities are made available at fixed prices. It is marked on the products.

Demerits

1. There are no salesmen. Any guidance that may be needed is not available.
2. Large capital is necessary, because it is located in big towns with more space.
3. The customers are allowed to handle the goods by themselves. It is also possible that some goods might be damaged.

The Government aims at starting many co-operative super markets to save the public in different cities. Example of co- operative super markets in Tamilnadu are, Kamadhenu Super Market in Chennai. Chinthamani Super Market in Trichy and Coimbatore and Karpagam Super Market in Vellore and Villupuram districts, and Ponni co-operative Super Market in Salem.

7.4 DIFFERENCES BETWEEN A CO-OPERATIVE SOCIETY AND A JOINT STOCK COMPANY

There are some points of similarity between a co-operative organisation and a joint stock company. Both secure capital by sale of share. Both are corporate bodies. In spite of this similarity the following are the important differences between the two.

S.No		JOINT STOCK COMPAY	CO-OPERATIVE SOCIETIES
1.	Meaning	It is mainly organised with the object of making profit. It is an association of persons formed for the purpose of doing a business	It is a voluntary association of the weaker section or the people. It may make profit in the prosess of rendering services.
2.	Minimum Number	There must be atleat two persons to form a private limited company and seven persons in public limited company.	But in the case of Co-coperative society, a minimum number of members is 25 as per the Tamilnadu co-operative Societies Act of 1983.
3.	Maximum Number	In a private company maximum is 50 and in a public company there is no maximum limit.	There is no limit to the maximum number of members in a Co-operative Society
4.	Local Membership	The members of a public limited company belong to different parts of the country and even different countries of the world.	But in a co-operative society the members belong to the same locality.
5.	Registration	A company is formed and registered as per the companies Act of 1956	But a co-operative society registered as per the Co-operative societies Act of a state government
6.	Management	In a joint stock company, the management is entrusted to the Board of Directors elected by the shareholders.	All the members are entitled to participate in the management of co-operative societies with the help of the Board of directors

1	2	3	4
7.	Object	Profit is the primary motto of a joint stock company.	Service is the primary motto of a Co-operative
8.	Purchase of Shares by member	In companies there is no limit in the purchase of maximum number of Shares	In Co-operative societies minimum number of purchase of shares is limited to the extent of utilisation of benifits.
9.	Facilities	Government do not provide any concession to joint stock companies as extended to co-operatives.	but a co-operative society enjoys concession like exemption from paying incometax, stamp duty and registration fee etc.
10.	Right to Vote	In joint stock company one share one vote principle is followed.	But in a co-operative society one man vote principle is followed.
11.	Feeling of self-interest	In a joint stock company the feeling of self interest and competition remain present.	In co-operative societies "Each for all and all for each" is the guiding principle.
12.	Repayment of shares Capital	A share holder cannot get back his capital during the life time of the company	A member in a co-operative society can surender his shares, withdraw his capital and cancel his membership
13.	Distribution of Profit	In joint stock company the profit is distributed to the shareholders on the basis of their share value.	In a co-operative society a minimum portion of the profit is distributed as dividend. A major portion of the profit is used for the development of the co-operative society
14.	Transfer of Shares	The shares are freely transferable in a public limited company.	A member of a cooperative society cannot transfer his shares. But he can surrender his shares.

1	2	3	4
15.	New Shares	When a company wants to increase its capital the new issue of shares are offered to the existing share holders if there is a Right issue.	in the case of co-operative society capital is generally increased when new persons are admitted as members.
16.	Exploitation	A joint stock company is a capitalistic enterprise. They try to exploit the public	But in the case of co-operative society it protects the poor from the exploitation of unscrupulous traders.
17.	Importance	In joint stock company money is more important than a man.	In a co-operative society man is more important than money.
18.	Registration of Membership	A company close the list of share holders as soon as the capital is fully subscribed. If any one wants to buy shares, he can buy them in stock exchanges.	In co-operative society the list of membership is not closed but open to all the members hailing from the society.
19.	Value of Shares	The value of shares is generally greater in joint stock companies. It may sell shares either at par, or at a premium and or at a discount.	But shares are offered only at par in a co-operative society.

Co-operative Movement in India

India is not a stranger to the idea of co-operation. Our ancient village economy was based on economic co-operation among the villagers. All the villagers co-operated in every activity in the village. References about Co-operation are made in Chanakya's ' Arthasastra'.

When the British started ruling our country, our old system of village management disppeared. But the modern Co-operative movement started only from 1904. Our farmers were very much indebted to the greedy moneylenders and traders. Their economic status was very pitiable. The Government wanted to help them. So the then Madras Government sent one official, Mr.Nicholoson, to Germany to study about the German Rural Credit Co-operatives. He recommended in 1895 that such Rural Credit Societies could be started in India also.

So in 1904, the Central Government passed the Credit Co-operative Societies Act. A number of Credit Co-operatives were started to lend money cheaply to the rural people. But this Act did not provide the starting of other types of Co-operatives or Central Co-operatives. So in 1912, the Government of India Passed a new Act called the Co-operative Societies Act. This Act provided for the starting of different types of Societies and also Federations of Co-operatives.

Under the Government of India Act of 1919, Co-operation became a Provincial (State) subject. Many provinces passed separate Acts to regulate the Co-operative Societies in their own Province (State). In Tamil Nadu the Madras Co-operatives Societies Act was passed in 1932. Now all Co-operatives in Tamil Nadu are regulated by the Tamil Nadu Co-operatives Societies Act, 1961.

POINTS TO REMEMBER

Introduction – History – Definition

- **Principles of co-operation.**

1. Voluntary organisation, 2.Equality. 3.Democratic management. 4.Combination & Resources. 5. Concentrated effort. 6.Sprit & service. 7.Plural membership. 8. Legal capacity. 9. Open membership. 10. Finance. 11. Limited return on capital. 12. Local membership. 13. No political influence. 14. State control. 15. Distribution of surplus. 16. Registration. 17.Separate legal entity. 18. Liability. 19.mutual help. 20. Statutory. 21. Cash trading. 22. No share transfer. 23. No speculation. 24. Corporate status. 25. Training in co-operation .

- **Merits**

1.Easy formation. 2. Unlimited membership. 3. Democratic management. 4. Limited liability. 5. Stability. 6. Economy in management 7. Cheper service. 8. Tax concession. 9. Special benefits. 10. Saving habit. 11. State patrange. 12. Eliminating middleman. 13. Fall in prices. 14. Employment. 15. Government help.

- **Demerits**

1. Inefficient management. 2. Limited capital. 3. Lack of motivation. 4. Lack of co-operation. 5. Domination of vested members. 6. Non-transferability of interest. 7. Lack credit of secrecy. 8. Excessive government control. 9. No credit facility. 10. No political rivalries.

- **Types of co-operation**

1.Credit societies - Agricultural credit societies, Rural credit societies, Nonagricultural credit societies - Urban banks - Employees credit societies, Worker credit societies, Non credit societies – co-operating marketing societies – co-operative farming societies

- **Industrial co-operatives.**

Non agricultural - Non-credit societies - consumer co-operatives - manufacturing co-operatives - Housing Co-operatives-Co-operative warehouses.

- **Differences between co-operatives societies and joint stock company.**

1.Meaning. 2. Minimum number. 3. Maximum number. 4. Local membership. 5. Registration. 6. Management 7. Object. 8. Purchase. 9. Facilities 10. Right to vote. 11. Feelings of self-interest. 12. Repayment of share capital. 13. Distribution of profit. 14. Transfer of shares. 15. New shares. 16. Exploitation. 17. Importance. 18. Registration of membership. 19. Value of shares

QUESTIONS

I. Select the correct answer

1. Co-operative society can be started

   a. Only at villages

   b. In towns and Villages

   c. Only in cities

   d. Only in urban areas

Ans:(b)

2. The minimum number of members required to form a co-operative society is

   a) 2 b) 7 c) 10 d) 25

Ans:(d)

3. Dividend is declared in a co-operative store to its members.

   a. Share capital b. Number of shares purchased

   c. Amount of patronage given d. None of the above

Ans: (c)

4. The basic objective of a co-operative society is.

   a. Earn profit

   b. Organise some essential service for the benefit of its member

   c. Organize essential services to the community.

   d. Arrange for enough of quality goods for the community

Ans: (b)

5. In a co-operative society, the shares of a member

   a. Can be transferred b. Can be repaid

   c. Cannot be transferred d. None of the above

Ans:(b)

6. Maximum membership in a co-operative society is

   a. 50 b. 60 c. 100 d. Unlimited

Ans: (d)

7. A co-operative super market supplies

   a. Credit b. service c. Goods d. Cash

Ans: (c)

8. Consumers co-operation was first successful in

   a. England b. USA c. Swiss d. India

Ans: (a)

9. Minority interest can be protected in

   a. Sole trader b. Partnership

   c. Co-operative societies d. Public Company

Ans: (c)

10. Central Co-operative bank is established at

   a. Villages b. Districts

   c. State head quarters d. Urban areas

Ans:(b)

II. Fill in the blanks

1. The Latin word co-operari means ______________________
2. The father of the co-operative movement was ___________________
3. Only __________________ of the profits to be distributed as dividend
4. The liability of the members of a Co-operative Society is ______________
5. Transfer of shares are possible in _____ and not possible in _____________
6. Management of a Co-operative Society is fully ______________________
7. Service is the main objective of _______________________
8. Agriculture credit societies are classified into

   a).Rural credit society

   b).___________________
9. An industrial co-operative is organized by ____________________
10. Super market refers to large scale __________________________

Answers:

1. To work with	2. Robert Owen
3. 14%	4. Limited
5. Joint stock company, Co-operative societies	
6. Democratic	7. Co-operative societies
8. Primary credit societies	9. Small scale producers
10. Retailing	

III. Match the following

1. Producers Co-operative	a. Cheap loans
2. Consumers Co-operative	b. Operating at district level
3. Co-operative Motto	c. Better Prices
4. State Co-operative Bank	d. A Portion of profit
5. Patronage dividend	e. Apex bank
6. Central Co-operative Bank	f. Roahdale pioneers
	g. Each for all, all for each

(Ans) 1 – c, 2 – f, 3 – g, 4 – e, 5 – d, 6 – b

IV. Short Questions

1. Define Co-operation?
2. Who are Rochdale pioneers?
3. What is meant by one man one vote?
4. What is the significance of ‘self help and mutual help’?
5. What are the aims of credit co-operative society?
6. Explain the meaning of ‘Consumer Co-operatives?
7. Give example of Co-operative super markets in Tamil Nadu?
8. What are the aims of Co-operative societies?
9. What do you understand by marketing co-operative?
10. What is agricultural credit society?
11. What is a co-operative warehouse?
12. Mention any four features of co-operative society?
13. What is a non-agricultural non-credit society?
14. What is Patronage Dividend?
15. Define Co-operative super market?

V. Paragraph Questions

1. Explain the types of agricultural credit societies.
2. Briefly explain the demerits of co-operative societies
3. What are the steps involved in forming a co-operative society?
4. State the meaning of super market and explain its features

VI. Essay Type Questions

1. Explain clearly the important features of co-operative organisation
2. Write the merits and demerits of a co-operative society
3. Distinguish between the joint stock company and co-operative society.
4. Explain any eight types of co-operative societies in detail.

CHAPTER - 8
GOVERNMENT IN BUSINESS

"The means of production should be socially

owned and controlled for the benefit of society as a whole".

Learning Objectives : After reading this chapter you will be able to understand the following.

- 8.1. The meaning, definition and objectives of state enterprises.
- 8.2.1. The meaning-features-merits and demerits of departmental form of organisation.
- 8.2.2. The meaning-features-merits and demerits of public corporation
- 8.2.3. The meaning-features-merits and demerits of government companies.
- 8.3. The differences between private sector and public sector.

8.1. INTRODUCTION

State Enterprise, as a form of business organisation gained economic importance in most of the countries of the world in recent years. During twentieth century, various governments started participating in industrial and commercial activities. Previously, the role of government was limited only to the maintenance of Law and Order. Industrial revolution helped all-round growth of industries.

Private entrepreneurs worked, only for profit motive. The exploitation of consumers and workers by private entrepreneurs became very common. The development of industries was left to the judgment of private enterprises. Therefore, Government control or intervention became a necessity to safeguard the interests of the general public, even in developed countries like U.S.A and U K. When the government cannot exercise effective control over private ownership for varied reasons, the only alternative is to take over such business units in the interests of the public.

DEFINITION

State enterprise is an undertaking owned and controlled by the local or state or central Government, for the welfare of the public at large. Either whole or most of the investment is provided by the government.

A.H. Hansen says "Public enterprise means state ownership and operation of industrial, agricultural, financial and commercial undertaking"

According to S.S. Kher, State Enterprises are "The industrial, commercial and economic activities carried on by the central or by a state government and in each case either solely or in association with private enterprise, so long it is managed by self – contained management".

The Government thus, can own and control industry and business in two ways:

(i) By starting a new unit.

(ii) By taking over an existing industrial or commercial unit owned by private persons.

OBJECTIVES OF STATE ENTERPRISES

State enterprises are established to implement economic policies of the government. The primary objective of the state enterprises is to serve the people and help in creating an environment for industrial activity. Main objectives of state enterprises are as follows:

1. Helping all-round Industrialisation

Private entrepreneurs will invest only in those industries where profit earning chances are more. They will not invest in an undertaking where profits are low irrespective of its utility for people. State enterprises are necessary for those lines where private sector is hesitant to invest. It helps in all-round industrialisation of the country.

2. Developing Basic Industries

Certain basic industries like iron and steel, chemicals are the most essential for economic growth. They must be developed only as state managed units.

3. Establishing Enterprises Requiring Heavy Investment

Some undertakings need heavy investment and the gestation period may also be longer. Private industrialists cannot afford to make such huge investments.

In case of railways, ship-building, energy producing concerns, etc very huge investments is required which is beyond the means of private investors. Hence, government enters these fields and establish its own undertakings.

4. To Provide Necessities

Government undertakes to provide various necessities like electricity, water, coal, gas, transport, communication facilities to the people. The aim is to provide these basic facilities at cheap rates. Private sector cannot be relied upon to provide these services. Moreover, there are chances of public exploitation in these services. So public utilities are provided by government undertakings.

5. To run Monopoly Sectors

Some industries are to be developed only in public sector. The industries like defence, nuclear energy etc. cannot be left in the private sector.

If defence industries are owned by private individuals / firm, in times of national emergency, they may not co-operate with the state. There is also the danger of defence secrets being given out to the enemy. So for the security of the country, defence Industries are always owned and managed by the state.

6. For Balanced Economic Growth

The aim of industrialisation is to develop all industries, essential for the country. Also, various regions of the country should be equally developed. Private sector may not establish industries in certain regions, where they do not find opportunities to earn more profit. They cannot be compelled to start their undertakings in backward regions. So government can start industries in backward areas.

7. For Exploitation of Natural Resources

Private sector will not like to risk capital in exploitating natural resources. Oil and natural Gas commission in India spends huge amount for finding out new sources of oil and gas. A private sector unit cannot spend such amounts on exploratory stages.

8. Preventing Concentration of Economic Power

If private sector is given a free hand, industrialization will lead to exploitation of consumers. It will ultimately lead to concentration of economic power in fewer hands. The existence of state/public sector will be a check on private sector.

9. Making for full Employment

Fullest employment is possible only under socialised production. No country has solved its ‘unemployment problem’ where the private sector is in full swing. The State, by proper centralised planning of industrial development, can aim at not only full employment of labour but also employment of all other available resources.

10. To increase Government Resources

Some of the state enterprises are run on commercial lines. The profits earned by such enterprises goes to the exchequer. Thus, it augments the resources of the Government which is ultimately directed for the development of the economic schemes of national importance and spent on social welfare schemes like education, medical help, housing, road building, etc., The welfare schemes will improve the economic conditions of all the people, especially the poor people.

11. For Establishing Socialistic Pattern of Society

Under socialistic pattern of society, the gap between rich and the poor is reduced and the means of production are controlled by the State. In capitalistic society the poor becomes poorer and the rich becomes richer. The establishment of a strong public sector is essential for the equal distribution of wealth.

8.2. FORMS OF ORGANISATION OF STATE ENTERPRISES

A suitable form of organisation will increase the efficiency of any industrial untertaking. Excessive dependence on government for finances will increase government interference in the day-to- day working. Enterprises should be run on business lines and necessary autonomy should be allowed to them.

The Government can organise an industrial or commercial unit in any one of the following forms:

(1) Department of the Government

(2) Separate Corporation.

(3) Joint Stock Company.

The choice of the particular form of organisation depends upon the nature of the industry, the circumstances of the country and the policy of the government.

8.2.1. Departmental organization

Department form of organisation of managing state enterprises is the oldest form of organisation. In those days, no distinction was made between the routine functions of the Government and that of the public enterprises. Therefore, most of the early state owned enterprises were the best examples of the departmental form of organisation. In India, Railways, Post and Telegraph, Radio and Television are working as government departments.

The finance for these organisations are wholly provided by the government and the management is in the hands of civil servants. The minister of the department is the ultimate in-charge of the enterprise. The enterprises is subjected to legislative scrutiny.

Features

1. Departmental undertakings are wholly dependent on government for finance.
2. The management of the enterprises is in the hands of the government. The enterprises are managed and controlled by the civil servants of a government department with a minister at the top. He is responsible to answer to the parliament for the operations of the undertaking.
3. The downward delegation of authority is effected from the top executive to every part of the organization i.e it represents the line authority relationship between the executives at various levels.
4. It is financed through annual budget appropriations made by the legislature. State treasury provides finances and surplus money (profits) is deposited in the treasury.
5. The affairs of the business are subjected to strict government budgeting, accounting and auditing. The accounting and audit control, applicable to other government departments are applicable to state enterprises also.
6. The departmental undertakings enjoy legal immunity i.e., it is part of the government. So, no legal action can be taken against it without the permission of the Government.

Merits

1. Complete Government Control

The control over the enterprise is direct and absolute. These undertakings are associated with one of the government department through which, government can regulate the working of these units in a proper way.

2. Management

The Civil Servants manage departmental organisations. These government officials will work sincerely and efficiently for the success of the unit.

3. Source of income for Government

These enterprises are run on commercial lines. The revenues of these enterprises directly go to the government for initiating other social and development activities.

4. Helps in implementing Government Policies

Government policies and programmes are better implemented by these enterprises under direct government control.

5. Proper use of Funds

Since these undertakings are subject to strict control, chances of misuse of funds are remote.

6. Secrecy

Strategic industries like defence and atomic power cannot be better managed other than government departments. Department undertakings can maintain secrecy in their working.

7. Useful for Specific industries

Departmental form of organisation is necessary for public utility services. The motive of these industries is not to earn profits but to provide services at cheap rates. Therefore, Post, Telegraph, Railways are in the form of government departments. Also, these are suitable for enterprises with long gestation period.

8. Legislative Control

These undertakings are under the control of legislatures or they are accountable to Parliament through the Minister. Legislative control acts as a check on functions of these undertakings.

Demerits

This type of organization is severely criticized by many, because of the several defects in it. They are:

1. Excessive Government interference

There is an excessive government interference and control in department organisation. These undertakings are not given freedom to decide their own policies. Centralised control leads to delay in action. Red-tapism and bureaucracy have become the limiting features of these organisations.

2. Shortage of Competent Staff

Civil Servants are given control of these undertakings who may not have business outlook or commercial experience. So, they run the undertaking in the their own fashion without considering the sovereignty of the consumers.

3. Centralisation of Powers

All policies are decided at ministerial level ignoring business consideration. Since a Ministry is responsible for full control over the departmental organisations, there may not be continuity in policy.

4. Delay and Red-tapism

There is too much of procedures which results in delay. Commercial organisation cannot afford delay in taking decisions.

5. Inefficiency

There is no competition to this business. Hence there is no economic compulsion to improve efficiency. Also, efficiency standards are not set for these undertakings. Losses in departmental undertaking are not taken seriously because they are run as government departments.

6. Political Changes

Since a ministry has control over the department, there may be no continuity in policy i.e., the change in government involves shift in policies of departmental undertaking.

7. Tax Burden to Public

Losses suffered by these undertakings will mean additional tax burden to the public. Tax revenue can only make up such losses.

8.2.2.Public Corporation

A public corporation is an autonomous body corporate created by a special statute of a state or central government. A public corporation is a separate legal entity created for a specific purpose. It is administrated by a Board appointed by public authority to which it is answerable.

FEATURES

1. Separate Legal Entity

A public corporation is established by a separate legislative Act passed by government (Central or State).

2. Perpetual Existence

It has perpetual existence and common seal. It can enter into contracts in its own name, acquire and hold assets and can sue or be sued without any government approval.

3. Government Investments

These corporations are fully financed by the government. In some cases private capital may also be associated but atleast 51percent of the shares to be held by the government.

4. Financial Autonomy

For day-to-day finance requirements, these corporations are not dependent on the government. They can borrow funds from public or government.

5. Management

It is managed by a Board of Directors. Generally, the board is nominated by the government of the basis of their experience and skill.

6. Service Motive

The motive of public corporations is to provide service to the public at a reasonable price.

7. Employees

Its employees are not government servants. The public corporations recruit their own employees. They can appoint capable persons to manage the corporation on commercial lines.

8. Power and Duties

The power, duties and responsibility of public corporation are fixed by the special Act establishing it.

9. No Government Interference

The government will not interfere in the day-to-day management of the corporation. They execute their independent policies.

10. Freedom of Action

There is freedom of action in financial management of public corporation. It is not subject to rigid government budgeting, accounting and audit controls. It can use its money for the purposes decided by its Board of Directors.

11. Accountability

A public corporation is accountable to the legislature, which created it and also to the ministry mentioned in the special Act. Its accounts are audited by Comptroller and Auditor-General and the Annual report is presented to the Parliament or Legislature.

12. Run on Commercial Lines

A public corporation is required to be run on commercial principles although profit is not the sole aim.

MERITS

1.Finance from Government

The public corporation gets share capital fully from government. It can borrow money from the public very easily at cheaper rate of interest.

2. Internal Autonomy

They can devise their own policies and programmes. They can set their own goals and can decide their own line of action.

3. Flexibility

Public corporation can manage its affairs with flexibility and initiative to suit business needs. The management is free to take decisions in the interest of the organisation.

4. Free from Government Interference

Public corporations are free from political interference, governmental delay, slow procedures etc. Various policies are decided independently.

5. Protect Public Welfare

The parliamentary and ministerial control over the broad policies and overall working of the corporation, will protect public welfare.

6. Run on Business Lines

These undertakings are run on commercial lines. It helps these to earn profit and finance their schemes and undertake expansion plans.

7. Accountability

Public corporations are accountable to the legislature for their performance. They try to increase their efficiency, otherwise they are criticised in the parliament or state legislature.

8. Service to Society

Public corporations provide commodities and services to the people at reasonable price. They also act as a model employer by providing maximum welfare facilities to their workers.

9. Management

The board of directors of these corporations consist of experienced persons (official and non-official) representing various sections of society. So the interest of all sections of the society are safeguarded.

DEMERITS

1. Limited Autonomy

In actual running of the corporation, the concerned government department/ ministry exercises direct or indirect control. All important policies are decided with government approval only. Management is appointed by the government. So, limited autonomy is only enjoyed by these corporations.

2. Difficulty in Making Changes

Any changes in the activities of the corporations need a change in the statute of the corporations. The statute can be amended only by a legislature. It is a difficult process and takes time to amend the statute.

3. Misuse of Powers

In many public corporations, the management have misused their freedom of action and worked beyond their powers. Financial autonomy of the corporation is sometimes, misused by the management. Public money may be wasted on unnecessary projects.

4. Inefficient

Public corporations in general have no competitors. So, they tend to become inefficient. The losses suffered by these corporations falls on the public as government has to give subsidies from exchequer to make up such losses.

5. Lack of Interest

Public corporations are managed by salaried employees. Since managerial personnel are also paid employees, they show no interest in the affairs of the corporation. Everything is managed in a routine way.

6. Government Control

Though these corporations are autonomous bodies, many controls are exercised by the government i.e., controlled through public accounts committee, Comptroller and Auditor General, etc.

8.2.3. GOVERNMENT COMPANY

A company owned by central and /or state government is called a Government company. Either whole of the capital or majority of the shares are owned by the government.

According to Indian Companies Act 1956, “Government company means any company in which not less than 51% of the paid-up share capital is held by the central government or by any state governments or government or partly by the central government and partly by one or more state government and includes a company which is a subsidiary of a government company”.

Government companies are registered both as public limited and private limited companies but the management remains with the government in both cases. Government companies enjoy some privileges which are not available for non-government companies. No special statute is required to form government companies.

Government companies enter those fields where private investment is not forthcoming. Sometimes, government has to take over sick units in private sector.

FEATURES

1. Incorporation

Government companies just like other companies in private sector are registered and incorporated under the Companies Act.

2. Government Finance

Most of the share capital or atleast 51% of the total share capital is held by the government. (Central or State or both)

3. Participation of Public

Public can also subscribe to the share capital of these companies, if offered to them.

4. Management

Government companies are managed by Board of Directors. The members of this Board are nominated by the government which holds the majority of the shares. Government nominates its representatives to different sectors like labour, foreign collaborators, technical experts, consumers, etc.

5. Autonomy

It is an autonomous unit with full freedom of action in financial and administrative matters.

6. Employees

The employees, except the officers deputed by the government, are not civil servants.

7. Control

The government company is under the overall control and supervision of the Minister under whose Ministry it is attached.

8. Auditor

The Auditor of a Government company is always appointed by the central Government.

9. Accountability

The annual reports of the company must be placed before both the houses of the parliament or legislature.

MERITS:

A government company, the most common form of organisation of State Enterprises has the following merits:

1. Easy to form

The formation of a government company is comparatively easy. No prior approval of the parliament/ legislature is required.

2. Flexibility in Management

There is flexibility in running the business of the company. It can follow flexible policy to suit the changing business conditions.

3. Freedom of action

It enjoys a large measure of freedom in matters of finance, administration and personnel. It can plan its own capital structure.

4. No government interference

It enjoys greater freedom and authority and is free from the protracted and time consuming regulations of the Government. So, the government company can work just like any private owned company.

5. Run on commercial lines

Government companies are run on sound business lines. They earn surpluses to finance their own expansion.

6. Expertise

Government company enables the government to procure and accommodate managerial skill, technical know-how of the private enterprise or foreign countries by conveniently collaborating with them.

7. Healthy competition

Government companies provide healthy competition to the private sector.

8. Helpful in developing neglected sectors

Private sector may not be coming forth to invest in certain sectors due to risk involved or less returns. But they are important industries from the national point of view. Government companies may enter these neglected areas and can help all round growth of the economy.

9. Efficiency

The working of the government companies is open to public criticism in the parliament / legislature. Hence, the management cannot avoid its responsibility.

DEMERITS

1. Political inference

In reality, government companies does not enjoy any autonomy in its activities. The interference of the Ministers has been very frequent. Every Government tries to nominate directors from its own political party and through these, companies are run on political consideration.

2. Minority interest neglected

Since government is the majority shareholder, the Government is able to impose its will on the management of such company.

3. Lack of interest

The top position officials of the company are not dedicated to the success of the company as they are frequently transferred. The Board of Directors also do not have necessary skill and experience to run the business on sound business lines.

4. Accountability

The Annual Audit Report placed before the Parliament reveal only financial matters. There is no accountability for the operational efficiency, administration, and personnel of the companies.

5. Red-Tapism

These companies are dependent on the government for taking important policy decisions. Red-tapism in governments affect the working of these companies.

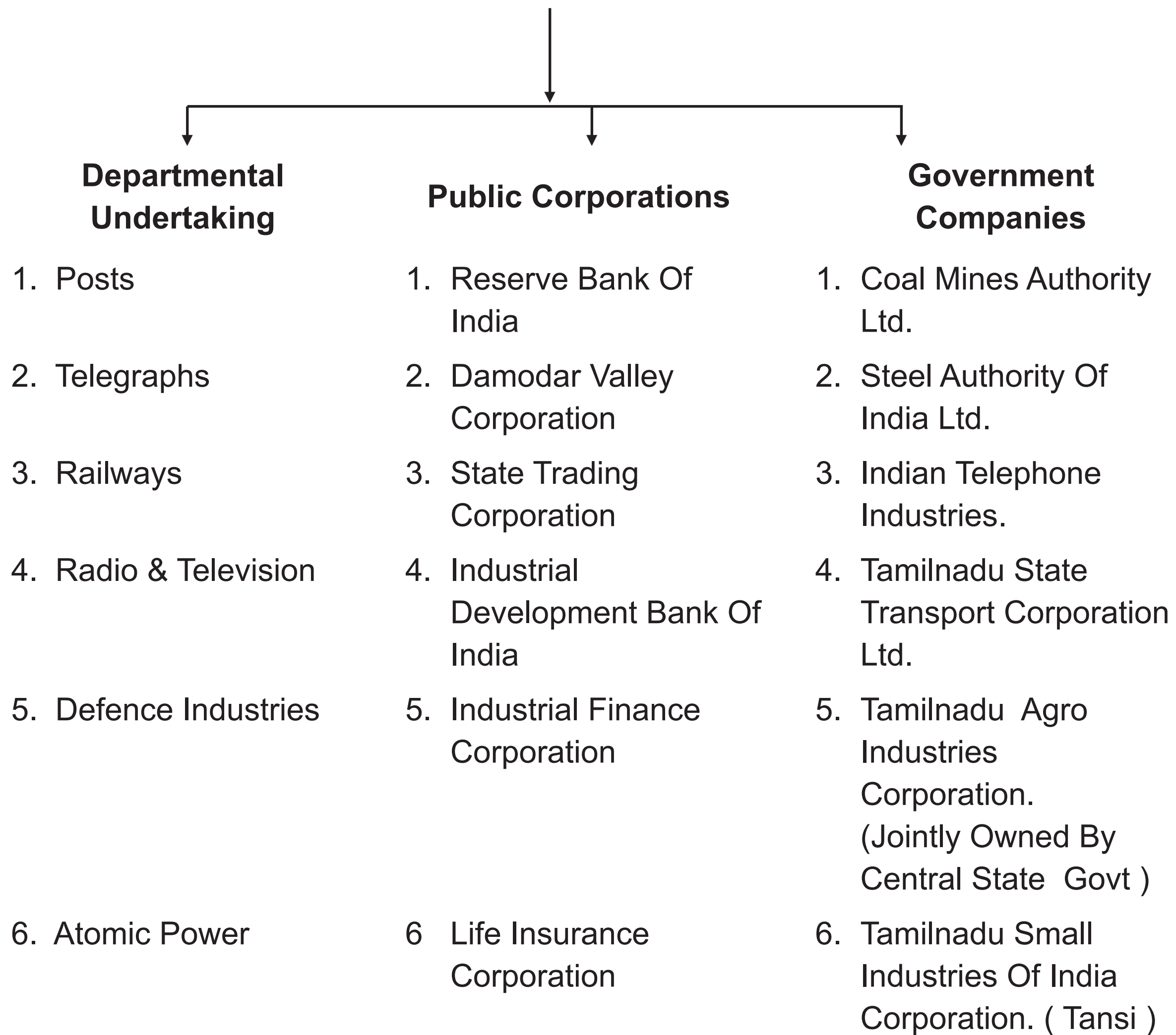
Government company form of organization is suitable in the following circumstances.

1. When the government wants to take over an existing enterprise in an emergency.
2. When the State wants to establish an undertaking in collaboration with private enterprises or with foreign countries
3. When there is a need for flexibility in the operations of the enterprises.
4. When the Government wishes to start the enterprises with a view of transferring it to private management later.

8.3 DIFFERENCE BETWEEN PRIVATE SECTOR AND PUBLIC SECTOR

S.No	Public Sector	Private Sector
1.	Service motive - with twin goal- achieve economic development with democratic values and economic equality.	Profit motive - maximise the profits.
2.	Sufficient, unlimited resources; successful in mobilizing savings through banks, bonds, etc.	Limited resources;The private sector is not successful in mobilising the resources of the country or from foreign countries for the economic development
3.	Checks concentration of economic power in the hands of few.	Leads to concentration of economic power in the hands of few individuals.
4.	Develop those sectors which are neglected by the private sector.	Develop those industries/ sector in which risk is less and returns is more.
5.	Preserves national wealth.	Exploitation of natural resources like forests, mines etc., for personal advantage.
6.	Brings in balanced growth; starts industries in backward area.	Do not establish industries in backward areas.
7.	Heavy, basic and defence industries are reserved for public sector.	Consumer goods industries, agriculture are in private sector.
8.	Consumer welfare is considered important. They are supplied goods and services at cheaper prices.	Consumers are exploited.
9.	Model employer. Solves unemployment problem to a great extent.	Exploitation of employees. Welfare of employees neglected.
10.	The managment of public sector industries are managed by civil servants . They lack efficiency/ skill to run public enterprises on commercial lines.	Technical qualification and experience of private owners is used for efficient management of private sector enterprises.

STATE ENTERPRISES



Departmental Undertaking	Public Corporations	Government Companies
1. Posts	1. Reserve Bank Of India	1. Coal Mines Authority Ltd.
2. Telegraphs	2. Damodar Valley Corporation	2. Steel Authority Of India Ltd.
3. Railways	3. State Trading Corporation	3. Indian Telephone Industries.
4. Radio & Television	4. Industrial Development Bank Of India	4. Tamilnadu State Transport Corporation Ltd.
5. Defence Industries	5. Industrial Finance Corporation	5. Tamilnadu Agro Industries Corporation. (Jointly Owned By Central State Govt)
6. Atomic Power	6 Life Insurance Corporation	6. Tamilnadu Small Industries Of India Corporation. (Tansi)

Points to Remember

Meaning

Government Undertakings are units owned and controlled by the central, State or both jointly.

❖ **Need for Government Undertakings.**

1. To regulate the economy 2. To accelerate economic development 3. To raise the standard of living of people 4. To prevent concentration of economic power 5. To improve job opportunities for unemployed.

❖ **Nature of Government Undertakings.**

1. For defence need 2.For public utilities 3. For development of basic industries 4. For providing essential services 5. For social welfare activities

❖ **Origin of Government Undertakings.**

In India since independence, there has been a tremendous growth in Government enterprises though its origin can be traced back to the period of Chola kings in 12th century.

❖ **Types of Government Undertakings.**

1. Departmental Enterprises 2. Statutory Corporations 3. Government Companies

❖ **Departmental Enterprises.**

These are organisation set up as departments of the government attached to a ministry to control the essential services sectors in the economy.

❖ **Features of Departmental Enterprises.**

1. Operates as a part of the Government ministry 2.Centralised control 3.Reporting of activities to concerned minister 4.Government finance 5.Source of revenue to the government 6. Strict accounting and auditing by the Government

❖ **Merits of Departmental Enterprises.**

1. Efficient operations 2. Profit center for government 3. Protects public interest 4. Loyalty of employees 5. Increased productivity

❖ **Demerits of Departmental Enterprises.**

1. Rigidity 2 Delay in decision making 3. Constant political interference 4. Limited managerial ability 5. Limited scope

❖ **Statutory Corporations**

These are organisations started by passing a special Act in the state of Central Legislative. It is a combination of Public ownership and public accountability.

❖ **Features of Statutory Corporation**

1. Incorporated by special Bills or Act in a parliament 2. Separate legal entity 3. State Control 4. Nominated directors of Government 5. Service Motive 6.Employment conditions fixed by corporation

❖ **Merits of Statutory Corporation.**

1. Autonomy of operation 2. Absence of political interference 3. Quick and prompt decision 4. Absence of exploitation 5. Easy way of raising capital.

❖ **Demerits of Statutory Corporations**

1. No flexibility in operation 2. Misuse of powers 3. Lack of efficiency 4. Not easy to alter activities 5. Political interference could be there.

❖ **Government Companies**

There are units started by the Government in the form of Joint Stock Companies under the provisions of the Indian Companies Act of 1956, with government owning 51% or more of the capital of the company.

❖ **Features of Government Companies**

1. Company form of organisation structure 2. State ownership 3. Directors nominated by the Government 4. Ministerial control 5. Government audit and accounting

❖ **Merits of Government Companies**

1. Easy formation 2. Flexibility in operation 3. Prompt decisions 4. Absence of political interference 5. Greater efficiency of operation

❖ **Demerits of Government Companies**

1. Absence of freedom of operation 2. Chances of misuse of power 3. Restricted growth 4. Constant political interference 5. Inefficiency in administration

❖ **General advantages of State Enterprises**

1. Balanced growth 2. Long period planning 3. Facilitates economic development 4. Greater public welfare 5. Equal distribution of wealth 6. Better co-ordination 7. Abolition of monopoly 8. Greater economy 9. Better relationship with labour force 10. Better deal to consumers 11. Utilisation of local resources 12. Achievement of self-reliance 13. Establishment of heavy and strategic industry 14. Balanced production and equitable distribution of wealth.

❖ **General disadvantages of State Enterprises**

1. Lack of initiation and efficiency 2. Lack of selection of goods 3. Political interference 4. Slow growth 5. Poor management 6. Lack of flexibility

QUESTIONS

I. Choose the correct Answer:

1. Government companies are registered under

   a) Special statute of Government b) Companies Act, 1956

   c) Royal charter d) Order of the Government

2. In a public corporation the management has

   a) Limited freedom b) No freedom of action

   c) Controlled freedom d) Unrestricted freedom of action.

3. For the efficient working of state enterprise the form of organisation generally considered suitable is

   a) Departmental organisation b) Public corporation

   c) Government company d) None of these

4. Public can also subscribe to the share capital of

   a) Public corporation b) Departmental undertaking

   c) Government company d) None of these

5. In a government company the share capital of the government must not be less than

   a) 51% b) 60% c) 75% d) 90%

Ans: 1 (b),2 (c), 3(b), 4 (c), 5 (a).

II. Fill in the blanks with suitable words:

1. ____________ is an undertaking owned and controlled by Government.
2. The primary aim of state enterprises is ________________
3. Public corporations are created by __________ of central or state Government.
4. In a Government company atleast ______________ shares are owned by the Government
5. The oldest from of public enterprise is _________________________
6. When the Government takes over an existing private concern it is called ______________
7. The most suitable form of organisation for manufacturing defence goods is___________________

8. ____________ checks concentration of economic power in the hands of few.

9. Exploitation of consumers and employees is a feature of _____________

10. Public corporations are managed by a _______ nominated by the Government.

Ans: 1. State enterprises. 2. Public welfare.
3. Special statute. 4. 51%.
5. Departmental organisation. 6. Nationalisation.
7. Departmental organisation. 8. Public sector.
9. Private sector. 10. Board of directors.

III. Match the following:

(i)

1. Atomic power	a. Legal immunity
2. Takeover of existing business by Government	b. Departmental undertaking
3. Departmental organisation	c. Indian telephone industries
4. Public corporation	d. Nationalisation
5. Government company	e. Damodar valley corporation
	f. 25% share holding by Government

Ans: 1 (b), 2 (d), 3 (a), 4 (e), 5 (c).

(ii)

1. 51% share holding by Government	a. Aim of state enterprises
2. Benefits of both Department organisation and Joint stock company	b. Departmental organisation
3. State control over industries	c. Companies Act
4. Railways	d. Special statute
5. Public corporation	e. Government company
	f. Public corporation

Ans: 1 (e),2 (f),3 (a),4 (b), 5 (d).

IV. Short Questions:

1. What was the role of Government in the past?
2. What necessitated Governments to intervene in industrial sector?
3. Define state enterprises?
4. How can we establish state enterprises?
5. How does the state enterprises bring in balanced economic growth?
6. What factors govern the choice of a particular form of organisation for an industry?
7. Why departmental organisation is suitable for defence industries?
8. Explain the management of public corporation?
9. Define a Government company.

V. Paragraph Questions:

1. State the features of the departmental form of state enterprises.
2. What are the features of a public corporation?
3. Explain the features of a Government companies.
4. What are the differences between public and private sector?

VI. Essay Questions:

1. Explain the objectives of state enterprises.
2. Discuss the features, merits and demerits of the Departmental organisations.

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