Business Types

Hello and welcome to another CanIndian Channel Feature. This video is part of Corporate Governance Section. Please feel free to watch other sections of MBA 101 course.

Before we dive into the topic of Corporate Governance we are first going to look at different types of business organizations. I will use examples associated with each type and use this as reference video for other sections of this segment.

There are three basic types of business organizations:

Corporation

Multi-owner business

Single owner business

The corporation is a business that is totally separate from its owners. The owners are shareholders. If you watched my leadership videos, I used an example where I used to work for a pizza store during my time as student. The pizza store was a part of a giant corporation called PizzaPizza Corp in Ontario Canada.

Multi-owner business: This type of business is owned by several individuals, includes partnerships. Again going back to my videos in Marketing where I talk about my business called iHappy Novelties. This business was started as a partnership with my friends. Little did we know it became a huge endeavor and with the profits we were able to buy gifts for families that couldn't afford it during Christmas and I was featured in the local newspaper. Yes, the dorky looking person is me with my actual show off swag.

Single-owner Business – The sole proprietor is owned by one person. This is my business called Sujabal Enterprise for which I am a consultant where I visit companies to optimize production efficiency.

Now let us look at incorporation:

Most business start as Sole proprietor or partnership and then spiral out to become incorporated such as a Corporation or Limited Liability company. In other words, it becomes a legal business entity of its own — separate from the individuals who founded it. The new company structure often falls into two categories: a limited liability company (LLC), or a corporation (corp).

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The reason a business moves from sole proprietor to limited liability company or corporation is to protect the individual's assets. It kinda puts a wall between your asset and company's asset. If the company goes bankrupt or gets sued it will not mean that the owners will lose their personal asset such as their home, car etc. LLCs are subject to fewer regulations than traditional corporations, and thus may allow members to create a more flexible management structure than is possible with other corporate forms. As long as it remains within the confines of law, the operating agreement is responsible for the flexibility the members of the LLC have in deciding how their LLC will be governed. Also, a customer and other business perceives LLC or Corporation as a more legitimate business and preferred than sole proprietorship. The main difference is LLC business cannot issue stocks, where are corporations can issues stocks. Due to the nature of the Corporations all financial information should be made public, this is not the case for LLC.

For the scope of this video we are only to look at corporate governance aspect on the various business type discussed. We will look at details of LLC's and Corporation on another segment. The reason I made this video is to provide fundamentals to future videos on this section and as stated before I will be using example that I listed earlier.

Thank you for watching this video. I look forward to seeing you on another video. This is CanIndian Channel signing off. Peace!!

Agency Theory

Hello and welcome to another CanIndian Channel Feature. This video is part of Corporate Governance Section. Please feel free to watch other sections of MBA 101 course.

In this video we are going to look at a very interesting concept called the Agency Theory. I assure you by the time you are done watching this video you will have a clear concept of what Agency Theory is.

Diving straight onto the topic, remember my previous video where I stated my friends and I used to own a business called iHappy Novelties. We used to sell light up items at events and shows. My friends and I used to hire other students to help us run the business. Within no time we became extremely successful and had operations all over the country. We then decided to hire senior staff; let's call them agents to look after the business. We were making extremely good money, so we let the managers run our business. We treated the managers well, paid them a fair share of profits. Somewhere along the line the managers started developing partnerships with the event authorities and started making and selling products that offered them higher commission. This affected our sales and soon enough our sales started to drop.

If we look at what happened my friends I who are the shareholders of the business decided to let the managers run the business. The agents became greedy and put their vested interest in front of them and started to do business that benefitted them the most. This is the basis of agency theory. In an agency relationship, agents are required to work toward meeting principals' goals, yet it is the agents' own goals that drive them to succeed on behalf of their principals. In order for an agency relationship to be mutually beneficial, both parties' goals must be addressed within a climate of compromise, but with the understanding that meeting the principal's goals is the primary function of the relationship. Now this example was for LLC.

Let's look at another example for Corporation. It was very nicely explained by G Chambers.

Say if we have shareholders purchase shares of a company. Basically, a group of people combine their money, issue shares and list it as a corporation. They hire directors to run the business for them. In this example the shareholders do not work in the day to day business and they rely on the directors to follow the duty of stewardship. I will discuss the stewardship theory on another video. Because the shareholders are not involved with the day to day business there is a distance of separation which creates a knowledge gap between the directors and shareholders. This creates the mistrust and misunderstanding. Also, this is an efficacy to basis of Agency Theory.

Agency theory has 2 following assumption:

1. *The agents are egoists*

2. *The agents make decision to their advantage.*

Now going back to our example. The director issue financial reports and issue it to the shareholders. As per Agency theory the report could be falsified. The directors could have forged number to his/her advantage. Hence to combat this concern the Shareholders can hire auditors or agents to ensure they audit the financial reports.

I really hope you now have a clear understanding of this theory. Please feel free to watch other sections of this corporate governance segment. Hope to see you on another video. This is CanIndian Channel signing off. Peace!!

Transaction Cost Theory

Hello and welcome to another CanIndian Channel Feature. This video is part of Corporate Governance Section. Please feel free to watch other sections of MBA 101 segment.

In this video we are going to be looking at a concept called the Transaction Cost Economics.

*The **theory of transaction cost economics**, also called social cost theory, is a contractual concept developed by British economist Ronald Coase in 1937 and refined by American economist Oliver Williamson in 1975. The theory addresses the importance of companies or firms in a market economy. It proposes that hierarchical organizations, like firms, may distribute resources more efficiently than an imperfect or limited bargaining system, like a market.*

To carry out a market transaction it is necessary to discover who it is that one wishes to deal with, to conduct negotiations leading up to a bargain, to draw up the contract, to undertake the inspection needed to make sure that the terms of the contract are being observed, and so on.

More succinctly transaction costs are:

- *search and information costs*
- *bargaining and decision costs*
- *policing and enforcement costs*

This is another topic that is not explained well in most academic's books or videos on the internet. I had to really dig deep into the original research article by Ronald Coase and then gain an understanding. Once understood, the topic and the result is quite interesting and useful. I promise, stay along with me and you will too benefit from this concept.

Ronald Coase gives the origin of <u>The Nature of the Firm</u> as a course in the organization of the business unit which he taught in 1932. He noted that there are inconveniences of market transactions, but if transactions are not governed by the price system there has to be an organization. The object of a business organization is to reproduce the conditions of a competitive market for the factors of production within the firm at a lower cost than the actual market. But if an organization exists to reduce costs then why is there any market transactions at all? Coase gave two reasons:

- *1. the costs of organizing additional transactions rise with scale and are equated with the costs of additional market transactions;*
- *2. the organization of bigger firms may not reproduce the effects of market conditions.*

Too much academic gibberish eh!

Alright let me explain this using an example and then you too will have an Eureka moment.

Remember my previous video where I talk about my business iHappy Novelties. The products that we sold mainly light up t-shirts, hats were also sold at a store called partycity in Canada. Initially iHappy Novelties was a small company basically sole proprietor. We did not have expenses such as search and information cost by agents, bargaining and sourcing cost and did not have any corporate lawyers review our paperwork. My friends & I basically visited Alibaba website ---trade secret revealed here. Where as party city had all those cost and their product needed to factor in those cost making their products expensive. This is a main basis of transaction cost economics. Now further on once the same products started appearing and public started noticing it, Walmart decided to sell them. Now due to the sheer size of Walmart purchase power they used the bargaining cost with supplier to drive the price down. We no longer could compete with Walmart and decided to move into another product.

I hope this made sense, please feel free to leave me a comment if you still have issues understanding this concept and I will try my best to explain this further. Any constructive criticism is also welcome.

As always thank you for investing your time in watching this video, I hope I added some value to your learning. See you on another video. This is CanIndian Channel signing off.

Peace!!!