Entrepreneurship, New Ventures, and Business Ownership

chapter three
After reading this chapter, you should be able to:

1. Define *small business*, discuss its importance to the U.S. economy, and explain popular areas of small business.
2. Explain entrepreneurship and describe some key characteristics of entrepreneurial personalities and activities.
3. Describe the business plan and the start-up decisions made by small businesses and identify sources of financial aid available to such enterprises.
4. Discuss the trends in small business start-ups and identify the main reasons for success and failure among small businesses.
After reading this chapter, you should be able to:

5. Explain sole proprietorships, partnerships, and cooperatives and discuss the advantages and disadvantages of each.

6. Describe corporations, discuss their advantages and disadvantages, and identify different kinds of corporations; explain the basic issues involved in managing a corporation and discuss special issues related to corporate ownership.
What Is a “Small” Business?

- **Small business**
  - one that is independent (not part of a larger business) and that has relatively little influence in its market

- **Small Business Administration (SBA)**
  - government agency charged with assisting small businesses
Almost 86 percent of all U.S. businesses have no more than 20 employees. The total number of people employed by these businesses is approximately one-fourth of the entire U.S. workforce. Another 29 percent work for companies with fewer than 100 employees.
The Importance of Small Business in the U.S. Economy

- Job creation
- Innovation
- Contributions to big business
Small businesses have accounted for about 40 percent of all new jobs in high-technology sectors of the economy.

Small businesses are generally the first to hire in times of economic recovery.
Figure 3.2 Small Business by Industry

- Services: 50.74%
- Retailing: 14.7%
- Construction: 11.16%
- Wholesaling: 5.6%
- Finance and Insurance: 6.83%
- Manufacturing: 3.46%
- Transportation: 2.75%
- Other: 4.76%
Entrepreneur

Entrepreneur

Entrepreneur

Entrepreneurship

Entrepreneurship

Entrepreneur

businessperson who accepts both the risks and the opportunities involved in creating and operating a new business venture

Entrepreneurship

the process of seeking business opportunities under conditions of risk
Entrepreneurial Characteristics

- Resourcefulness
- Concern for good, personal customer relations
- Strong desire to be their own bosses
- Deal with uncertainty and risk
Business plan

Document in which the entrepreneur describes her or his business strategy for the new venture and demonstrates how it will be implemented.
Crafting a Business Plan

- Setting Goals and Objectives
- Sales Forecasting
- Financial Planning
1. What are the entrepreneur’s goals and objectives?
2. What strategies will be used to obtain them?
3. How will these strategies be implemented?
Starting the Small Business

- Buying an Existing Business
- Franchising
- Starting from Scratch
Franchise
- an arrangement in which a buyer (franchisee) purchases the right to sell the good or service of the seller (franchiser)
Franchising

Advantages
- Proven business opportunity
- Access to management expertise

Disadvantages
- Start-up costs
- Ongoing payments
- Management rules and restrictions
Starting from Scratch

- Who and where are my customers?
- How much will those customers pay for my product?
- How much of my product can I expect to sell?
- Who are my competitors?
- Why will customers buy my product rather than the product of my competitors?
Financing the Small Business

- Personal resources
- Loans from family and friends
- Bank loans
- Venture capital companies
- Small-Business Investment Companies (SBICs)
- Minority Enterprise Small-Business Investment Companies (MESBICs)
- SBA financial programs
Financing the Small Business

- **Venture Capital Company**
  - group of small investors who invest money in companies with rapid growth potential

- **Small-Business Investment Company (SBIC)**
  - government-regulated investment company that borrows money from the SBA to invest in or lend to a small business
Emergence of E-Commerce
   - The Internet provides fundamentally new ways of doing business

Crossovers from Big Business
   - More businesses are being started by people who have opted to leave big corporations and put their experience to work for themselves

Opportunities for Minorities and Women
Trends in Small-Business Start-Ups

➢ Global Opportunities
   - Many entrepreneurs are also finding new opportunities in foreign markets

➢ Better Survival Rates
   - Today, 44 percent of new start-ups can expect to survive for at least four years
Figure 3.4 Reasons Women Give for Starting Businesses

- Gain control over my schedule: 46%
- Saw a market opportunity and decided to pursue it: 24%
- Frustrated with "glass ceiling" at big companies: 23%
- Other reasons: 7%
Reasons for Failure

1. Managerial incompetence or inexperience
2. Neglect
3. Weak control systems
4. Insufficient capital
Reasons for Success

1. Hard work, drive, and dedication
2. Market demand for the products or services being provided
3. Managerial competence
4. Luck
Noncorporate Business Ownership

- **Sole Proprietorship**
  - business owned and usually operated by one person who is responsible for all of its debts

- **General Partnership**
  - business with two or more owners who share in both the operation of the firm and the financial responsibility for its debts
Sole Proprietorship

Advantages
- Freedom
- Simple to form
- Low start-up costs
- Tax benefits

Disadvantages
- Unlimited liability
- Limited resources
- Limited fundraising capability
- Lack of continuity
Partnerships

➤ Advantages

- More talent and money
- More fundraising capability
- Relatively easy to form
- Limited liability for limited partners
- Tax benefits

➤ Disadvantages

- Unlimited liability for general partners
- Disagreements among partners
- Lack of continuity
### TABLE 3.1 Comparative Summary: Three Forms of Business

<table>
<thead>
<tr>
<th>Business Form</th>
<th>Liability</th>
<th>Continuity</th>
<th>Management</th>
<th>Sources of Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proprietorship</td>
<td>Personal, unlimited</td>
<td>Ends with death or decision of owner</td>
<td>Personal, unrestricted</td>
<td>Personal</td>
</tr>
<tr>
<td>General Partnership</td>
<td>Personal, unlimited</td>
<td>Ends with death or decision of any partner</td>
<td>Unrestricted or depends on partnership agreement</td>
<td>Personal by partner(s)</td>
</tr>
<tr>
<td>Corporation</td>
<td>Capital invested</td>
<td>As stated in charter, perpetual or for specified period of years</td>
<td>Under control of board of directors, which is selected by stockholders</td>
<td>Purchase of stock</td>
</tr>
</tbody>
</table>
Alternatives to General Partnerships

- **Limited Partnership**
  - Allows for limited partners who invest money but are liable for debts only to the extent of their investments
  - General (or active) partners run the business

- **Master Limited Partnership**
  - Master partner has majority ownership and runs the business; minority partners have no management voice
Cooperatives

➤ Combine the **freedom** of sole proprietorships with the **financial power** of corporations

➤ Groups of sole proprietorships or partnerships agree to work together for their **common benefit**
Proportions of U.S. Firms in Terms of Organization Type and Sales Revenue

Figure 3.5 Proportions of U.S. Firms in Terms of Organization Type and Sales Revenue

- Percentage of Businesses:
  - Corporations: 70%
  - Partnerships: 11%
  - Sole Proprietorships: 19%

- Percentage of Sales Revenue:
  - Corporations: 85%
  - Partnerships: 10%
  - Sole Proprietorships: 5%
The Corporate Entity

Corporation

A business that is legally considered an entity separate from its owners and is liable for its own debts; owners’ liability extends to the limits of their investments.
Corporations

Advantages
- Limited liability
- Continuity
- Stronger fundraising capability

Disadvantages
- Can be taken over against the will of its management
- Double taxation of profits
- Complicated and expensive to form
### Types of Corporations

<table>
<thead>
<tr>
<th>Type</th>
<th>Distinguishing Features</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Closely Held</td>
<td>Stock held by only a few people</td>
<td>Blue Cross/Blue Shield</td>
</tr>
<tr>
<td></td>
<td>Subject to corporate taxation</td>
<td>MasterCard</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Primestar</td>
</tr>
<tr>
<td>Publicly Held</td>
<td>Stock widely held among many investors</td>
<td>Dell Computer</td>
</tr>
<tr>
<td></td>
<td>Subject to corporate taxation</td>
<td>Starbucks</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Texas Instruments</td>
</tr>
<tr>
<td>Subchapter S</td>
<td>Organized much like a closely held corporation</td>
<td>Minglewood Associates</td>
</tr>
<tr>
<td></td>
<td>Subject to additional regulation</td>
<td>Entech Pest Systems</td>
</tr>
<tr>
<td></td>
<td>Subject to partnership taxation</td>
<td>Frontier Bank</td>
</tr>
<tr>
<td>Limited Liability</td>
<td>Organized much like a publicly held corporation</td>
<td>Pacific Northwest Associates</td>
</tr>
<tr>
<td></td>
<td>Subject to additional regulation</td>
<td>Global Ground Support</td>
</tr>
<tr>
<td></td>
<td>Subject to partnership taxation</td>
<td>Ritz Carlton</td>
</tr>
<tr>
<td>Professional</td>
<td>Subject to partnership taxation</td>
<td>Norman Hui, DDS &amp; Associates</td>
</tr>
<tr>
<td></td>
<td>Limited business liability</td>
<td>B &amp; H Engineering</td>
</tr>
<tr>
<td></td>
<td>Unlimited professional liability</td>
<td>Anderson, McCoy &amp; Orla</td>
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<tr>
<td>Multinational</td>
<td>Spans national boundaries</td>
<td>Toyota</td>
</tr>
<tr>
<td></td>
<td>Subject to regulation in multiple countries</td>
<td>Nestlé</td>
</tr>
<tr>
<td></td>
<td></td>
<td>General Electric</td>
</tr>
</tbody>
</table>
Corporate Governance

roles of shareholders, directors, and other managers in corporate decision making and accountability
Corporate Governance

- **Stockholder (or Shareholder)**
  - owner of shares of stock in a corporation

- **Board of Directors**
  - governing body of a corporation that reports to its shareholders and delegates power to run its day-to-day operations while remaining responsible for sustaining its assets

- **Officers**
  - top management team of a corporation
Special Issues in Corporate Ownership

- Joint Ventures and Strategic Alliances
- Employee Stock Ownership Plans
- Institutional Ownership
- Mergers, Acquisitions, Divestitures, and Spin-Offs
Applying What You’ve Learned

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