UNIT 5 - HOW ARE BUSINESSES ORGANIZED? (6 Days)

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3. Lessons from Financial Fitness for Life are on VE. They also have educational technology tools that can be found here: https://www.econedlink.org/resources/collection/fffl-9-12/

When most students enter the workforce they will work for a business or start their own business. So, it's important for them to understand the basics of how businesses work. Some people want to own their own company so they can be their own boss and just work when they want to. What they find is that they will be working many more hours than if they worked for someone else--because all of the responsibility falls on them. Other folks form partnerships; generally the partners bring resources to the company as well as different skills. Partnership has the difficulty of shared decision-making. Both forms have unlimited liability--so the owners personal assets are on the line.

Some businesses organize as corporations. With corporations, the owners are shareholders. Many large corporations are publicly traded; that is, their shares can be bought and sold on stock exchanges such as the New York Stock Exchange, the American Stock Exchange and the NASDAQ. They answer to their shareholders. Each form of business has advantages and disadvantages for the owners. Shareholders, for example, have limited liability for actions of the corporation.

All businesses must earn profits to continue--whether they are sole proprietors, partners or corporations. This impacts what prices they charge for the goods or services they produce. It also impacts who they hire and what salaries they pay.

EPF.2 The student will demonstrate knowledge of the role of producers and consumers in a market economy by
d) comparing the costs and benefits of different forms of business organization including sole proprietorships, partnership, corporation, franchise and cooperative
(BUS6120.043)

Day 1 and 2 Proprietorship, partnership, franchise, cooperative, corporation—what are the characteristics as well as the advantages and disadvantages of each?

EPF.18 The student will demonstrate knowledge of investment and savings planning by
f) describing how the stock market works
(BUS6120.137)

Day 1 Some corporations go public
Day 2 How are stock prices determined?

<u>EPF 2 The student will demonstrate knowledge of the role of producers and consumers in a market economy by</u>
h) describing the effects of competition on producers, sellers and consumers
(BUS6120.047)

Day 1 What are the characteristics of competitive and less competitive markets?

Evaluation Day

Day 1 and 2 - Proprietorship, partnership, franchise, cooperative, corporation—what are the characteristics, advantages and disadvantages of each?

Content Knowledge

The role of an economic system is to get goods and services produced for the members of a society. In a market economy businesses produce most of the goods and services—based on what consumers are willing and able to buy. Businesses may be small or large, have many owners or just a few. Owners consider the advantages and disadvantages of the various forms of business and are free to decide which works best for them.

Vocabulary
Cooperative – A legal form of business owned by the people who use its services or by the people who work there.
Corporation – A legal entity owned by shareholders whose liability for the firm's losses is limited to the value of the stock they own.
Franchise – A form of business in which one owner uses the model, methods and trademarks of another.
Partnership – A business with two or more owners who share the firm's profits and losses.
Proprietorship – A business with one owner who takes full responsibility for the firm's profits and losses.

Virginia Board of Education Framework
Sole Proprietorship

> ***Benefits***: The owner makes all decisions and keeps all profits.
> ***Costs:*** The owner generally has limited financial resources. The owner also faces unlimited liability, which means if the company fails, the owner can lose personal assets along with business assets.

Partnership

> ***Benefits*****:** Owners make decisions and keep the profits. They share responsibilities, and each has a unique set of skills and expertise.
> ***Costs:*** Owners face unlimited liability, limited financial resources, and potential conflict with partners.

Corporation

> ***Benefits***: Corporations are able to accumulate sufficient financial capital to make large-scale investments and achieve economies of scale (i.e., bringing down cost of production by producing in volume). They also have limited liability, meaning shareholder risk is limited to their share of ownership in the corporation. The corporation transcends the lives of those persons who created it.
> ***Costs:*** Corporations face tax implications (e.g., double taxation—profits are taxed at the corporate level and again when distributed to shareholders as dividends). Corporations are more expensive to establish and are governed by more regulations.

Cooperative

__Benefits:__ Cooperatives are member-owned and operate for members' benefit (e.g., credit unions, agricultural cooperatives). Members enjoy discounted products and/or services, may receive refunds at the end of the year, face no personal liability, have a vote in how the business is run, and have interests similar to other members.

__Costs:__ Decisions made by the group may not suit all members, and the decision-making process may be more complex and slower than in other organizations.

Franchise

__Benefits:__ Training and marketing is provided by the franchisor. The franchisee gains the exclusive right to sell in an area and benefits from product development.

__Costs__: The franchisee pays high franchise fees, enjoys a limited product line, and operates under strict guidelines and standards.

Most businesses in the United States are organized as sole proprietorships. Corporations generate the most income.

Teaching Tips

1) Ask students what kind of work they plan to do when they get out in the world. Suggest there are really only three types of places they can work. See if they can come up with—*business (including owning one's own business), government or non-profit organization*. Have students write down the three categories. In groups have them decide what percentage of the workforce is employed in each category. Remind them that their answers must total 100%. Write the three categories on the board. As each group reports, write their answers under the correct heading. Expect them to be surprised when you tell them that approximately 17% work for government (state, local and federal), 10% for non-profits and 75% work for a business.[1] Conclusion: It's important to understand how businesses work because you will probably work for one or even own one.

2) Introduce the main forms of business with the advantages and disadvantages of each.

3) Discussion points: Students should be asked to suggest advantages and disadvantages of each form of business. Sole proprietorship and partnership are two organizational forms. In the discussion, you can suggest that sharing has both an up-side and a down-side and ask the students what would be the up-side and down-side of sharing for each factor. For example, if the business needs to replace a machine that has quit working, what are the advantages of having a partner or partners? What are the disadvantages of having a partner or partners? If the business has an extremely good year, what is the advantage of having a partner or partners? What is the disadvantage of having a partner or partners?

[1] Data from OECD "Government at a Glance 2015" (https://www.oecd-ilibrary.org/governance/government-at-a-glance-2015_gov_glance-2015-en) and the Bureau of Labor Statistics (https://www.bls.gov/opub/ted/2014/ted_20141021.htm).

Franchise is a form of business that many students are probably aware of. Explain that with franchises, certain decisions are limited to the franchising company (franchisor) and others are the responsibility of the franchisee. For example: the owner of a McDonald's franchise has certain restrictions on what they can offer on the menu. They are also restricted to purchasing certain products from certain suppliers.

The last two forms of business allow for a greater number of owners – the corporation and the cooperative. The corporation was designed as a way to raise large quantities of capital by involving a greater number of owners (stockholders). The advantage of the corporation is that the firm becomes a legal entity or person in its own right. And the liabilities of the firm are limited to the assets of the firm itself. The stockholder's loss is limited to the capital invested through the purchase of stock, while the profit potential is theoretically limited only by the success of the corporation.

Cooperatives are also multi-owner and limited liability firms. They differ from corporations in that the firm's owners are either the customers or the employees of the firm. Students may be most familiar with the customer-owned cooperative as this is the model of most credit unions. (Costco and Sam's are not cooperatives. They do have members, but the members do not own the company.) In both cases, the instructor should make an effort to demonstrate how liabilities are limited through this form of ownership and compare it to the more extensive liability of a proprietorship or partnership.

4) Give examples of businesses in various situations; let students decide which business form would meet the needs of that business.

5) Look up data on which form of business most companies choose. *(Sole Proprietorship)* What form of business has the greatest total sales? *(Corporation)*

Lessons and Resources

Focus: Institutions and Markets Lesson 3: Business Organizations

Online Readings
[Article about cooperative ownership] What Millions of Retiring Small Business Owners Could Mean for Cities https://nextcity.org/daily/entry/what-millions-of-retiring-small-business-owners-could-mean-for-cities

Five Steps Before Investing in a Pet Franchise
https://www.franchising.com/articles/5_steps_to_take_before_investing_in_a_pet_franchise.html

Day 1 - Some corporations go public

Content Knowledge

Financial markets include banks and insurance as well as the stock and bond markets. Some corporations grow so quickly that they don't have enough money to finance the growth. They may choose to sell shares of their company (stock) to raise money to expand. The people who buy those shares of stock become part owners. If the company is profitable the shares will pay dividends and increase in value. Sometimes a company will go out of business altogether and their shares become worthless. However, because it is a corporation, the shareholders have limited liability. Shareholders can only lose the money they have invested. They have no additional liability.

Vocabulary
Corporation - A legal entity owned by shareholders whose liability for the firm's losses is limited to the value of the stock they own.
Stock - An ownership share or shares of ownership in a corporation.
Stock Market - A market in which the public trades stock that someone already owns; the buying and selling of stock.
Bond - A certificate of indebtedness issued by a government or a publicly held corporation, promising to repay borrowed money to the lender at a fixed rate of interest and at a specified time.
Shareholder - One who owns one or more shares of stock
Dividend - A share of a company's net profits paid to stockholders.
IPO - A company's first sale of stock to the public. When a company "goes public," it sells blocks of stock shares to an investment firm that specializes in initial offerings of stocks and resells them to the public.
Primary Market - The market where new securities are offered for sale for the first time. Investment banks buy shares of stocks directly from corporations that issue them and sell these shares to others.
Secondary Market - A market in which stocks can be bought and sold once they are approved for public sale; for example, the New York Stock Exchange.

Virginia Board of Education Framework
EPF 18f: When companies make profits, they may keep the profits to help them grow or they may share the profits with shareholders in the form of dividends. Shareholders can make money through dividends or through capital gains. A capital gain occurs when one sells a share for more than one paid for it.

Teaching Tips

1) Ask students if they know the difference between stocks and bonds. Perhaps some have participated in the Stock Market Game or own stock of their own. Define the two terms. Explain that people who own stock share in the success and failure of a business. If the business is profitable, the value of its shares may rise (so the owner may be able to sell for more than he/she

paid) and the company may distribute dividends from the profits of the company. In contrast to the ownership represented by stock, when one buys a bond it is like making a loan to a company and earning a specific rate of return. The bondholder expects to receive that interest whether the company does well or poorly.

2) Review limited liability as one of the advantages that corporations enjoy. Why is this important with respect to the stock market? (*People would be reluctant to buy stock if it meant taking on the liabilities of the company.*) Why is it important to have a stock market? (*People also would be reluctant to buy stock if they had to go find someone to buy their stock when they wanted to sell. Also, the market tells just how much buyers and sellers think a stock is worth*.)

3) Explain that nearly all corporations started out as small companies and grew. When a company first comes to market it is called an IPO (Initial Public Offering). Have students research current public offerings. Did any companies on the New York Stock Exchange start in your community?

4) Look up companies which are headquartered in Virginia and listed on the New York Stock Exchange, American Stock Exchange or the NASDAQ.

5) Time permitting, participate in a simulation that walks students through an IPO.

Lessons and Resources

Learning, Earning and Investing for a New Generation Lesson 10: Financial Institutions in the U.S. Economy.

Learning, Earning, and Investing for a New Generation Lesson 3: What is a Stock?

Khan academy on what it means to buy a company's stock (13:46)
http://www.khanacademy.org/video/what-it-means-to-buy-a-company-s-stock?playlist=Finance

"What is a company," from *The Stock Market Game*

"What is a stock?" from *The Stock Market Game*

Day 2 - How are stock prices determined?

Content knowledge

Who sets the price of a stock? Like most other things that are sold in a market economy, the price of stock is set by supply and demand. Something in the news makes people want to buy a particular stock. This is an increase in demand. If everything else remains the same, the demand curve will shift to the right and the price will rise. Suppose there is bad news about a company.

Some shareholders will decide to sell. This brings more stocks to the market for sale—an increase in supply. The supply curve shifts to the right and the price of the stock goes down.

Stock prices are based on expectations. If investors expect the price of a stock to go up, they will want to buy. This brings an increase in demand. If investors expect that the price of a stock is going down, they may decide to sell. That would result in an increase in supply. What investors expect determines supply and demand and the price of stock.

Vocabulary
Demand - The quantity of a good or service that buyers are willing and able to buy at all possible prices during a period of time.
Expectations - What consumers or businesses anticipate will happen, especially concerning markets and prices.
Stock - An ownership share or shares of ownership in a corporation.
Stock Market - A market in which the public trades stock that someone already owns; the buying and selling of stock.
Supply - The amount of a good or service that producers are willing and able to offer for sale at each possible price during a given period of time.

Virginia Board of Education Framework
EPF 18f: Stock prices are determined by supply and demand based on investor expectations. If a company is expected to be profitable in the future, demand for its shares rises and the price rises; when a company's future looks less-than-profitable, demand decreases and the price falls.

When the overall economy is robust and growing, people become optimistic about prospects for business and the stock market goes up. Likewise, when investment interest rates fall, the stock market generally rises.

When interest rates rise, the market goes down. When the overall economy is in decline, investors lose confidence and the stock market goes down.

Teaching Tips

1) This is an opportunity to show how supply and demand work in the real world. Use this time to review and practice using supply and demand curves to show how prices are determined in the stock market.
2) Define expectations. Explain how the expectations of buyers and sellers of stock affect prices in the stock market.

3) Prepare cards which read "supply" "demand" "increase" "decrease" "right" "left". Give each group a set of these cards. Practice with newspaper headlines such as the following and demonstrate on a supply and demand graph. Think about how the event will affect stock buyers' and stock sellers' expectations about the future profitability of the company.

"Analysts predict that Coca Cola profits will be higher than expected due to international sales."

Is this likely to affect supply or demand? *(both)* Will there be an increase or decrease in demand for Coca Cola stock? *(increase)* Will the demand curve shift to the right or to the left? *(right)* Will there be an increase or decrease in the supply of Coca Cola stock for sale? *(decrease)* Will the supply curve shift to the right or to the left? *(left)* Will the price of Coca Cola stock increase or decrease? *(increase)*

"The XYZ company has been sued for patent infringement." Will this affect supply or demand? *(both)* Will there be an increase or decrease in the supply of XYZ stock for sale? *(increase)* Will the supply curve shift to the right or to the left? *(right)* Will there be an increase or decrease in the demand for XYZ stock? *(decrease).* Will the demand curve shift to the right or to the left? *(left)* Will the price of XYZ stock increase or decrease? *(decrease)*

Continue using current news events. Help students think about events from the perspective of both the stock buyer and the stock seller. For every trade, there must be both a buyer and seller. One party thinks it's a good time to sell while the other thinks it's a good time to buy. They have differing expectations.

Lessons and Resources

EconEdLink Lesson : "Buy and Hold: A Stock Market Simulation."
https://www.econedlink.org/resources/buy-and-hold-a-stock-market-simulation/

Learning, Earning and Investing for a New Generation Lesson 14: How Are Stock Prices Determined?

Ecedweb "What is a stock? or Who Owns McDonalds"
https://www.unomaha.edu/college-of-business-administration/center-for-economic-education/teacher-resources/6-8/who-owns-mcdonalds_.pdf

NGPF NextGen Personal Finance Lesson 24: ANALYZE: What's the S&P 500?
https://docs.google.com/document/d/17r7G2VTMLEtI0zjw111HMfiouL72kIiqSXzvEOlqh3k/edit

Simulation
The Stock Market Game in Virginia – Student teams manage a $100,000 portfolio and can compare their results with other teams in the region and the state. Recognition is given to the teams with the highest portfolios after a state period of time.
http://www.vcee.org/programs-awards/view/4
The Stock Market Game
http://www.smgww.org/

Day 1 - What are the characteristics of competitive and less competitive markets?

Content Knowledge

Competition makes athletes improve by pushing them to do better. Competition does the same thing to businesses. Businesses work to produce better products at lower prices in order to attract customers. Consumers benefit from this. Businesses also benefit from competition when they can choose to buy their supplies from a variety of competing sources, which keeps their costs down.

Some industries are more competitive than others. When there are many buyers and many sellers, no one has market power. This is a very competitive market structure. On the other hand, a monopoly has only one seller and it can use its market power to raise prices and reduce the quantity it brings to market. Oligopoly has a few sellers. Monopolistic competition has many sellers, but is different from perfect competition.

Because competition has benefits to consumers, such as lower prices, more choices, and better quality, the government seeks to keep competition in industries. There are laws against monopolizing and collusion which reduce competition.

Vocabulary

Barriers to entry - Factors that restrict entry into an industry and give cost advantages to existing firms. Examples would include the large size of existing firms, control over an essential resource or information, and legal rights such as patents and licenses.

Competition - Attempts by two or more individuals or organizations to acquire the same goods, services, or productive and financial resources. Consumers compete with other consumers for goods and services. Producers compete with other producers for sales to consumers.

Differentiation – Making a non-price distinction between the features or characteristics of one's product or service from those of similar products and services.

Industry - An industry is a distinct group of productive or profit-making enterprises sharing similar products or services (e.g., the automobile industry).

Monopolistic Competition - A market structure in which slightly differentiated products are sold by a large number of relatively small producers, and in which the barriers to new firms entering the market are low.

Monopoly - A market structure in which there is a single supplier of a good or service. Also, a firm that is the single supplier of a good or service for which there are no close substitutes; also known as a monopolist.

Natural Monopoly - An industry in which the advantages of large-scale production make it possible for a single firm to produce the entire output of the market at a lower average cost than a number of firms each producing a smaller quantity.

Oligopoly - A market structure in which a few, relatively large firms account for all or most of the production or sales of a good or service in a particular market, and where barriers to new firms entering the market are very high. Some oligopolies produce homogeneous products; others produce heterogeneous products.

Perfect - Competition A market structure in which a large number of relatively small firms produce and sell identical products and in which there are no significant barriers to entry into or exit from the industry. Firms in perfect competition are price takers and in the long run will earn only normal profits.

Virginia Board of Education Framework
Competition among producers and sellers leads to more choices, improved quality, and lower prices as producers seek to attract customers away from other businesses.
Competition among consumers leads to higher prices and allocates goods to those willing to pay the most (e.g., several buyers bidding at an auction push the price up).

An industry is a distinct group of productive or profit-making enterprises sharing similar products or services (e.g., the automobile industry). The level of competition in an industry is affected by the ease with which new producers can enter the industry and by consumers' information about the availability, price, and quantity of substitute goods and services.

Markets with perfect competition have many buyers with perfect information and sellers all selling identical products. Sellers here have no market power—no control over the market price. (For example, a grower of plain white rice can only sell at the market price; no one will pay more because they can get plain white rice from any supplier at that price.)

Teaching Tips

1) Discuss the benefits of competition to consumers. Discuss the benefits of competition to businesses.

2) Ask students if businesses like having competitors. *(Businesses would rather be monopolies—so they wouldn't have the pressure of competition. But they like competition among their suppliers.)*

3) Draw a continuum on the board with perfect competition at one end and monopoly on the other. Describe and discuss each of the market structures. Explain that the continuum shows degrees of competition.

perfect competition	**monopolistic competition**	**oligopoly**	**monopoly**
Many buyers and many sellers Homogeneous product No market power Low barriers to entry	Many buyers and many sellers Differentiated product	Few sellers Price leadership High barriers to entry Homogeneous or differentiated product	One seller Unique product High barriers to entry

In perfect competition sellers have no control over the market price. Their product is identical to all others of the same type (homogeneous) —for example winter rye, feed corn. The market price is set by supply and demand for the product and each supplier has to take the market price--suppliers have no market power to set the price. Buyers will pay no more than the market price to get the product from one seller when they can get the same product from other sellers at the market price. This is the market structure farmers face. When good weather brings a bumper crop the increase in supply may result in a market price that is actually below what it costs the farmer to grow the crop.

Looking at the other end of the continuum, ask students for examples of monopoly *(in some places cable TV, electrical power, popcorn in movie theaters).* How are monopolies able to keep competitors out? There are barriers to entry such as patents, copyrights, control of resources, high cost of getting into the business. Discuss prices and sensitivity to customer convenience where there are monopolies. Define natural monopoly. Why does government regulate the price of electricity and cable tv? *(To keep companies from taking advantage of being the single supplier and charging a high price).* Compare monopoly to perfect competition.

There are market structures in between. Oligopoly is a market structure where a few companies dominate an industry—think soft drinks, cereal, detergents, and automobiles. Observe that soft drink makers make many different drinks—but there are just a few companies. One of the characteristics of oligopoly is "price leadership." Because there are so few companies they can watch and follow one another. In 2011 some large banks began charging for debit card use. When customers complained, and other big banks did not follow, those who started the trend had to stop the practice or lose customers to banks who did not charge those fees. Similarly, one airline started charging for checked luggage—and, with few exceptions, other airlines quickly followed.

Monopolistic competition sounds like it should be most like monopoly—but it's really most like perfect competition. The chief difference is differentiation. There are many sellers in this industry and they differentiate (point out the difference, often in advertising) their goods or services in hopes that consumers will pay a bit more for them. Examples would be restaurants, auto repair shops, hotels, hair salons.

4) Suppose that all the gas stations in town got together and agreed on one price. Would that be a good thing or a bad thing for consumers? For gas station owners? Why is collusion unlawful? Why would businesses want to collude? When the Organization of Petroleum Exporting Countries (OPEC) established a cartel to control oil prices through managing the supply of oil, this was an example of collusion.

Lessons and Resources

Capstone Lesson 22: How Competitive is the Industry?

High School Economics Lesson 4: A Classroom Market for Cocoa.
http://hseconomics.councilforeconed.org/

Videos
"Real World Economics – Market Structure" (13:00)
http://www.dailymotion.com/video/x871gq_real-world-economics-market-structu_school

mjmfoodie - Episode 25: Market Structure (5:51)
http://www.youtube.com/watch?v=9Hxy-TuX9fs (about competitive and uncompetitive markets)

Stossel: The Fight Against Food Trucks http://reason.com/reasontv/2017/12/12/stossel-the-fight-against-food-trucks

Emily Smith "Types of Markets" https://www.youtube.com/watch?v=QJnP8jzBjvk

Article
"Competition in the Food Truck Industry." https://www.dummies.com/business/start-a-business/competition-in-the-food-truck-industry/

"Study Explores the Impact of Uber on the Taxi Industry"
https://www.forbes.com/sites/adigaskell/2017/01/26/study-explores-the-impact-of-uber-on-the-taxi-industry/#601855ea16b0

"Competition in the Banking Industry Comes From an Unexpected Source."
https://mobilebusinessinsights.com/2017/03/competition-in-the-banking-industry-comes-from-an-unexpected-source/

EVALUATION DAY