Not-for-profit organisations

A number of organisations are run according to business principles, but do not aim to make a profit. They are known as NOT-FOR-PROFIT ORGANISATIONS. Their proceeds or surpluses from trading may be shared with employees and customers or passed on to a third party. Such organisations may be involved in a range of business activities. They may also employ staff, raise finance, buy resources, sell goods or services, market themselves, have a formal structure and be required to meet the needs of different stakeholders. They have to operate within the law and may also be faced with competition. Not-for-profit organisations include the following:

- public sector organisations;
- co-operatives;
- mutual organisations;
- charities;
- pressure groups.

Co-operatives

The origins of Co-operatives The UK Co-operative Movement grew from the activities of 28 workers in Rochdale, Lancashire. In 1844 they set up a retail co-operative society - The Rochdale Equitable Pioneers Society. With capital of just £28 they bought food from wholesalers and opened a shop, selling 'wholesome food at reasonable prices'. The surplus (or profit) made was returned to members of the society in the form of a 'dividend'. The dividend was in proportion to how much each member had spent. The principles of the society were:

- voluntary and open membership;

Figure 1: The Co-operative's business activities

Food The largest community food retailer in the UK with more than 2,200 stores, over 52,000 employees.
Healthcare Has more than 700 outlets and 5,000 employees. It is the third largest pharmacy business in the UK.
Travel The UK's most diverse retail travel business, with more than 450 high street branches, strong internet, call centre and home working businesses as well as significant cruise, franchise and business travel operations.
Funer alcare The UK's largest funeral business with over 800 funeral branches and in excess of 3,500 employees.
End of Life Planning A newly established End of Life Planning business which aims to grow its stake in the funeral planning market.
Sunwin Motors One of the top 25 motor businesses in the UK, with a turnover of £250 million and 22 showrooms in Yorkshire, Lancashire and the East Midlands.
Cash In Transit Provides services for over half of The Co-operative Bank's ATM estate.
E-Store Operates several e-commerce sites and provides electrical buying, warehousing and distribution services for the Co-operative Movement.
The Co-operative Legal Services Offers free advice and legal help for members of The Co-operative Group on everything from buying or selling a property to will writing.
Property Responsible for property assets including an investment portfolio which is largely invested in the retail and commercial property sectors.
The Co-operative Farms The largest farmer in the UK with over 70,000 acres of farmland in England and Scotland. They supply products such as soft fruit, cider, potatoes and packet flour to The Co-operative food stores.
Shoefayre A leading footwear and accessories retailer with over 1,700 employees and 240 stores throughout the UK.

Mandate A leading designer, manufacturer and distributor of corporate clothing.
Co-operative Financial Services (CFS) An Industrial and Provident Society, which brings together Co-operative Insurance (CIS), The Co-operative Bank and the internet bank Smile under common leadership.
The Co-operative Bank A bank famous for its ethical stance and high standards of customer service.
CIS/Co-operative Insurance A major life assurance and general insurance business with over four and a half million customers.
Smile An award-winning full-service internet bank.

Source: adapted from www.co-operative.co.uk.
Unit 9

- democratic ownership - one member, one vote;
- the surplus allocated according to spending (the dividend);
- educational facilities for members and workers.

Modern co-operatives Most modern co-operatives operate as CONSUMER or RETAIL CO-OPERATIVES. They are owned and controlled by their members. Members can purchase shares which entitles them to a vote at Annual General Meetings. The members elect a board of directors to make overall business decisions and appoint managers to run day to day business. Co-operatives are run in the interests of their members. Any surplus made by the co-operative is distributed to members as a dividend according to levels of spending. Shares are not sold on a stock exchange, which limits the amount of money that can be raised.

On Sunday 29 July 2007, the two main arms of the Co-op, The Co-operative Group and United Co-operatives, merged. The new society, called ‘The Co-operative’, is the world’s largest consumer co-operative with a turnover of more than £9 billion, 4.5 million members and 87,500 employees. The new organisation operates over 4,500 trading outlets throughout the UK. Figure 1 gives a summary of The Co-operatives’ business activities.

Worker co-operatives

Another form of co-operation in the UK with common ownership is a WORKER CO-OPERATIVE. This is where a business is jointly owned by its employees. A worker co-operative is an example of a producer co-operative where people work together to produce a good or service. Examples might be a wine growing co-operative or a co-operative of farmers producing milk.

In a worker co-operative employees are likely to:
- contribute to production;
- be involved in decision making;
- share in the profit (usually on an equal basis);
- provide some capital when buying a share in the business.

In 2006 there were less than 400 worker owned and controlled co-operatives in the UK according to Co-operatives UK. One example is the Edinburgh Bicycle Co-operative, a cycle retailer. One advantage of a worker co-operative is that all employees, as owners of the business, are likely to be motivated. Conflict will also tend to be reduced as the objectives of shareholders and employees will be the same. Worker co-operatives can involve the local community, either by giving donations to local bodies or even having them as members of the co-operative. However, there may be problems when operating as a worker co-operative.

- It is often difficult to persuade other workers to join a worker co-operative because it is much easier to set up a partnership.
- Some workers, new ones for example, may not want to join. They may not be able to afford the share.

Question 1.

Suma is an independent wholefood wholesaler-distributor. It specialises in vegetarian, fairly traded, organic, ethical and natural products and also has its own successful brand of food and non-food products. Suma operates as a workers' co-operative and has a truly democratic system of management that isn't bound by the conventional notions of hierarchy that often hinder progress and stand in the way of fairness. It uses an elected Management Committee to implement decisions and business plans but the decisions themselves are made at regular General Meetings with the consent of every co-operative member. There's no chief executive, no managing director and no company chairman. In practice, this means that their day-to-day work is carried out by self-managing teams of employees who are all paid the same wage, and who all enjoy an equal voice and an equal stake in the success of the business.

Source: adapted from www.suma.co.uk

(a) Using this case as an example, explain what is meant by a workers co-operative.
(b) Explain the likely effect on worker motivation at Suma of operating as a workers co-operative.

- Successful worker co-operatives often get sold to companies and the workers are happy to ‘sell out’ due to the lucrative offers made.
- Fresh capital cannot be raised by recruiting new shareholders. This often limits growth.
- Difficulties might be encountered when trying to recruit highly skilled and qualified staff. They may want more money then the equal wages being paid to existing members.

Building and friendly societies

Most building societies and friendly societies in the UK are MUTUAL ORGANISATIONS. They are owned by their customers, or members as they are known, rather than shareholders. Profits go straight back to members in the form of better and cheaper products. Friendly societies began in the 18th and 19th centuries to support the working classes. Today friendly societies offer a wide range of ‘affordable’ financial services. These include savings schemes, insurance plans and protection against the loss of income or death. They also provide benefits such as free legal aid, sheltered housing or educational grants to help young people through university. These extra benefits are distributed free of charge, paid for by trading surpluses. The government gives friendly societies special tax treatment, which reduces the amount of tax that members pay.

Building societies used to specialise in mortgages and saving accounts. Savers and borrowers got better interest rates than those offered by banks. This was possible because building societies were non-profit making. In the 1980s building societies began to diversify and compete with banks. In the late 1990s a number of building societies, such as Halifax, Alliance and Leicester, and Northern Rock, became public limited companies.
Factors affecting the choice of organisation

Age Many businesses change their legal status as they become older. Most businesses when they start out are relatively small and operate as sole traders. Over time, as needs change, a sole trader may take on a partner and form a partnership. Alternatively, a sole trader may invite new owners to participate in the business, issue shares and form a private limited company. Public limited companies are often formed from established private limited companies that have been trading for many years.

The need for finance A change in legal status may be forced on a business. Often, small businesses want to grow but do not have the funds. Additional finance can only be raised if the business changes status. Furthermore, many private limited companies ‘go public’ because they need to raise large amounts for expansion.

Size The size of a business operation is likely to affect its legal status. A great number of small businesses are usually sole traders or partnerships. Public limited companies tend to be large organisations with thousands of employees and a turnover of millions or billions of pounds. It could be argued that a very large business could only be run if it were a limited company. For example, certain types of business activity, such as oil processing and chemical manufacturing, require large scale production methods and could not be managed effectively as sole traders or partnerships.

Limited liability Owners can protect their own personal financial position if the business is a limited company. Sole traders and partners have unlimited liability. They may, therefore, be placed in a position where they have to use their own money to meet business debts. Some partnerships dealing with customers’ money, such as solicitors, have to have unlimited liability in order to retain the confidence of their clients.

Degree of control Owners may consider retaining control of their business to be important. This is why many owners choose to remain as sole traders. Once new partners or shareholders become a part of the business, the degree of control starts to diminish because it is shared with the new owners. It is possible to keep some control of a limited company by holding the majority of shares. However, even if one person holds 51 per cent of shares in a limited company, the wishes of the other 49 per cent cannot be ignored.

The nature of the business The type of business activity may influence the choice of legal status. For example, household services such as plumbing, decorating and gardening tend to be provided by sole traders. Professional services such as accountancy, legal advice and surveying are usually offered by partnerships. Relatively small manufacturing and family businesses tend to be private limited companies. Large manufacturers and producers of consumer durables, such as cookers, computers and cars, are usually plc’s. The reason that these activities choose a particular type of legal status is because of the benefits they gain as a result. However, there are many exceptions to these general examples.
Mergers and takeovers

efficiency gains were no greater than in non-merged businesses and in some cases were worse. This may have been because of a fall in turnover as the merged company rationalised its factory and cut output. Also profits of the combined company may have been lower than what they would have been without the merger.

Many of the businesses involved in mergers and takeovers, however, suggest that cost savings are the main reason for merging together. Some even produce figures to indicate the cost savings they would make. Examples of the economies of scale to be gained were:

- the elimination of duplicated resources. For example, cost savings from the merger between BP and Amoco in 1998 were to be gained from not duplicating oil exploration. The takeover of Amersham in the UK by Nycomed, a Norwegian biotechnical firm, resulted in savings of £9 million one year later;
- the reduction of risk. A small company may be reluctant to operate in a politically unstable country. The BP-Amoco merger may have been willing to do so, because it would have had other projects which may have been profitable if it had problems in certain countries;
- the spreading of the fixed costs of promotion. For example, the design of an advertisement or promotion is a fixed cost. An advertisement may cost £200,000 to make. If it reaches 1 million people in the UK, the average cost is 20p (£200,000 ÷ 1,000,000). If it is shown to 10 million people in the US the average cost falls to 2p;
- the ability to sell a wider range of products because of a wider sales network. This is known as one stop shopping or cross selling. Selling more products from the same distribution network will again reduce the average fixed cost of the sales network;
- the discovery by merged companies which have become global operators that their suppliers have also set up in many countries in which they operate;
- the fact that larger businesses are in a stronger position to negotiate with suppliers and can negotiate to reduce prices;
- the fact that merged businesses may have COMPLEMENTARY ASSETS. John Kay (1996) suggested that businesses may only be able to operate in certain markets if they have certain assets. For example, a business may advertise nationally to create a brand name. This is unlikely to be successful if it only has shops in Newcastle. It needs a complementary asset such as a chain of national shops.

Joint ventures and alliances

A JOINT VENTURE is where two or more companies share the cost, responsibility and profits of a business venture. The financial arrangements between the companies involved will tend to differ, although many joint ventures between two firms involve a 50:50 share of costs and profits. There are many examples of joint ventures. In 2007, Royal Dutch Shell plc and HR Biopetroleum announced the construction of a pilot facility in Hawaii to grow marine algae and produce vegetable oil for conversion into biofuel. Shell and HR Biopetroleum formed a joint venture company, called Cellana, to develop the project, with Shell taking the majority share. Construction of the demonstration facility on the Kona coast of Hawaii Island began immediately. In another 2007 deal, leading European passenger transport group Arriva plc entered into a new joint venture, which contracted to acquire 49 per cent of Italian bus operator SPT Linea for €6.8 million (£4.7 million). Arriva's Italian business SAB Autoservizi s.r.l. and Lombardy-based Ferrovie Nord Milano Group (FNM SpA), entered into a 50:50 joint venture to acquire the shares in SPT Linea. There is a number of advantages of joint ventures.

- They allow companies to enjoy some of the advantages of mergers, such as growth of turnover, without having to lose their identity.
- Businesses can specialise in a particular aspect of the venture in which they have experience.
- Takeovers are expensive. Heavy legal and administrative costs are often incurred. Also, the amount of money required to take over another company is sometimes unknown.
- Mergers and takeovers are often unfriendly. Most joint ventures are friendly. The companies commit their funds and share responsibility. Such an attitude may help to improve the success of the venture.
- Competition may be eliminated. If companies co-operate

Question 1.

Activision and Blizzard, the gaming companies behind Call of Duty and World of Warcraft, are to merge in a deal worth $18.8 billion (29.15 billion). US-based Activision also makes console games such as the Tony Hawk series and Guitar Hero. Blizzard is the biggest player in online gaming and World of Warcraft is the global market leader of what are known as massively multi-player online role-playing games. Blizzard is currently owned by the French media group Vivendi. As part of the merger plan, Blizzard will invest $2 billion in the new company, while Activision is putting up $1 billion. The merged business will be called Activision Blizzard and its chief executive will be Activision's current CEO Bobby Kotick.

The two firms are hoping that their different strengths will combine to form a business which is powerful on every gaming platform and in every territory. Blizzard is strong in Asia, where its Starcraft series has proved hugely popular. Starcraft, a strategy game first released in 1998, is played by millions of South Koreans in gaming cyber-cafés, and by professional gamers on television. Activision has a presence on all three new generation game consoles - Microsoft's Xbox 360, Sony's PlayStation 3 and the Nintendo Wii - with franchises such as Spider-Man and X-Men.

Source: adapted from https://bbc.co.uk.

(a) Using this case as an example, explain what is meant by horizontal integration.

(b) Why do you think Activision and Blizzard have merged?
in a joint venture they are less likely to compete with each other. However, the venture must not restrict competition to such an extent that consumers’ interests are harmed. There are some disadvantages to joint ventures:

- Some joint ventures fail to achieve the desired results. They are often compromised when an all-out takeover would be better. There may be control struggles. For example, who should have the final say in a 50:50 joint venture?
- It is possible for disagreements to occur about the management of the joint venture. As with any partnership, sometimes there are different views on which course of action to take.
- The profit from the venture is obviously split between the investors. A company might regret this if it became evident at a later date that a particular venture could have been set up by itself.

Alliances may take looser forms than joint ventures. They are usually for three reasons:

- Marketing. For example, McDonald’s and Disney have promoted each other’s products.
- R&D, where businesses work together to develop a new product. Each business will be able to contribute its individual expertise.
- Information. Supermarkets gather information on customers’ buying habits which they share with food manufacturers. This is perhaps a form of forward vertical integration.

**Demerging**

A DEMERGER is where a company sells off a significant part of its existing operations. A company might choose to break up to:

- raise cash to invest in remaining sections;
- concentrate its efforts on a narrower range of activities;
- avoid rising costs and inefficiency through being too large;
- take advantage of the fact that the company has a higher share valuation when split into two components than it does when operating as one.

In 2006, Severn Trent, Britain’s second-largest listed water company, demerged its Biffa waste disposal business in the UK. Biffa, valued at around £1 billion, was floated on the stock market on 6 October 2006. The company said there was little synergy between Biffa and its water and waste water business, and shareholders, customers and employees would benefit from dividing the two operations. It also said that £576 million of the proceeds would be returned to shareholders by means of a special dividend.

**Management buy-outs**

A MANAGEMENT BUY-OUT is where the ownership of a business is transferred to the current management team. The team is likely to buy shares from the existing owners. Funds for the buy-out might be provided by members of the management team itself or by financial institutions, such as banks or venture capitalists. Venture capitalists, such as CinVen, 3i and Schroder Ventures, are specialists who are prepared to take the risk of investing directly in a business. The capital they provide is sometimes called risk capital. Some buy-outs involve these venture capitalists taking complete control. This is known as a leveraged buy-out.

What might account for the popularity of management buy-outs?

- Many buy-outs occur when large companies restructure...