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# Chapter 21

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## Getting Started

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### Unit 5

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#### Higher Level

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#### Past Exam notes (For this chapter)

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## WHY START A BUSINESS

The main reason for someone setting up a business includes the following -

### 1. Independence

Many entrepreneurs prefer to be their own boss and make all the important decisions. Working as an employee may not give them the authority that they want so setting up a business will give them the control that they are looking for.

### 2. Profit

They will get to keep all the profit that the business makes. This means that they will be able to provide a high standard of living for themselves and their family.

### 3. Challenge

Entrepreneurs need to be challenged and reach their full potential. They like the challenge of starting a business and making it a success. They have an inner desire for success.

### 4. Creativity

They have the creativity of developing new innovative ideas and feel that starting a business is the best way to achieve their vision. They may feel that someone else may not have the same vision as them resulting in the idea not reaching its full potential.

### 5. Employment

They may have lost their job so have decided to open a business to help pay the bills. They may also be able to create employment for others which can help develop the local economy and improve the standard of living in the community.

Once a business idea has been identified the following must be decided

1. Legal Structure
2. Source of Finance
3. Production options

## WHAT ARE THE MAIN OWNERSHIP OPTIONS FOR A BUSINESS

There are 4 main ownership options available to an entrepreneur. These are -

<b>Sole Traders</b>	Def These are businesses that are opened and managed by one person.
<b>Partnerships</b>	Def These are businesses that have between 2 and 20 people. They come together to make a profit.
<b>Private Limited companies</b>	Def These are businesses registered with the Companies Registration Office (CRO) and are owned by shareholders.
<b>Co-operatives</b>	Def These are businesses that are democratically owned and controlled by their members. The members may be workers, suppliers or customers.

## MAIN FORM OF LEGAL STRUCTURE AVAILABLE

### 1. Sole Trader

#### Formation

- a) Can set up the company tomorrow if using their own money. If not will have to register their name with the Companies Registration Office.
- b) Must register with Revenue for tax.

#### Ownership & Control

- a) The company is owned and controlled by the sole trader.

#### Management & Finance

- a) All the decisions are made by the sole trader.
- b) Raising finance for expansion can be difficult.

#### Profit & Risk

- a) The sole trader gets to keep all the money but pays income tax on earnings.
- b) A sole trader has unlimited liability. This means that if they can't pay back a debt, they can lose their personal assets which will be sold to pay the money back.

### 2. Partnership

#### Formation

- a) Same as the sole trader - Can set up the company tomorrow if using their own money. If not will have to register their name with the Companies Registration Office.
- b) Must register with Revenue for tax.

### Ownership & Control

- a) The company is owned and controlled by the partners.

### Management & Finance

- a) All the decisions are made by the partners.
- b) Raising finance for expansion is easier by bringing in new partners. This dilutes the business means you lose more control and more people get a share of the profits.

### Profit & Risk

- a) The partners get to keep all the money but pay tax on their earnings.
- b) Partners have unlimited liability. This means that if they can't pay back a debt, they can lose their personal assets which will be sold to pay the money back.

## **3. Private Limited Company**

### Formation

- a) They have to register with the Revenue Commissioners.
- b) They also have to register with the Companies Registration office.

### Ownership & Control

- a) The business is owned by the shareholders who elect a board of directors to run the company and make the decisions.

### Management & Finance

- a) Decisions are made by the board of directors.
- b) Finance can be raised by selling shares.

### Profit & Risk

- a) Profits are shared among shareholders according to the number of shares they have.
- b) The company pays corporation tax with the shareholders paying income tax on the dividend they receive.
- c) Shareholders have Limited Liability. This means that they only lose the money they invest in the business and not their personal assets.

## **4. Co-operative**

### Formation

- a) This is the same as a private limited company - They have to register with the Revenue Commissioners.
- b) They also have to register with the Companies Registration office.

### Ownership & Control

- a) The company is owned by members who elect a management committee.

### Management & Finance

- a) Decision are made by a management committee.

### Profit & Risk

- a) Profits are shared among members equally.
- b) The Co-op pay corporation tax and member pay income tax on dividends.
- c) Share holder have Limited Liability. These means that they only lose the money they invest in the business and not their personal assets.

### Challenges new business face selecting an organisation structure.

Entrepreneurs must decide on the best ownership structure of the business. They must take into account the type of business they are operating, the number of owners involved and the tax and administrative implications of their choice

## BUSINESS LOCATION

This is where to situate the business - in a city centre or outside. It is a very important decision because it will affect if the business will succeed and how profitable the business will be. The following are some of the factors a business must consider when locating a business -

### **1. Proximity to your market**

Your business should be close to your target market, so it is convenient for you customer. This is important if you are a service business like a hairdresser. This is the place element from the Marketing Mix.

### **2. Proximity to your raw materials**

If your business is an iron or steel manufacturing business than it might be important to locate near a port or at least has access to good infrastructure for the goods to be delivered.

### **3. Transport and Communication links**

Access to ports and road networks are critical factors in locating a business. Especially if the business is in international trade. A communication network is also important to some business

trading in e-commerce. This might be a problem if you are in a rural area due to poor internet and broadband connections.

#### 4. Availability of skilled labour

If your business needs employees than you may located near them, so it is convenient for them to get to work. Some businesses will located near universities so they will have access to a skilled labour force. If the business can't get skilled worker, they may need to relocate at a huge cost

#### 5. Cost and availability of land

Land is becoming more and more scarce which is forcing the price of land and rents upwards. This can have an added cashflow pressure on business if they locate in a city.

#### 6. Waste disposal

Firms that produce a lot of waste should seek to locate near recycling or somewhere they can dispose of their waster safety especially if they use chemicals. Under a European Union directive waste must be disposed of close to the area where it was generated. This may end the practice of Irish waster being exported.

#### 7. Government Incentives

This is when the government gives incentives and grants for companies to located in less developed areas. This can reduce the costs for the business. The government can also use tax incentives to attract businesses to certain areas. For example, the IFSC (Irish Financial Service Centre)

**Foot loose** <sup>Def</sup> This is a business that is not tied down to locating in a particular area and can set up anywhere.

### WHAT FACTORS TO BE CONSIDER WHEN CHOOSING A SOURCE OF FINANCE

The following are some of the factors that should be looked at before getting a source of finance -

1. Purpose - The finance should match the purpose of the loan. If the loan is to be repaid before one year, then short-term source of finance should be used. The reason for the

finance must be considered. Is the finance required for the day-to-day running of the business or to finance business expansion? Short term needs must be financed from short term sources (e.g. Acquiring stock may choose bank overdraft or trade credit). Long term needs require long term sources of finance (equity, debentures)

2. **Amount** - The finance can vary considerably in terms of the amount. So, it is important that you borrow the right amount, so you are not paying back extra in interest. Also, if large amounts are required, generally a long-term source of finance is chosen as you can spread the costs over a longer period of time.
3. **Cost** - How much will the interest repayments be and how will this affect profitability and production costs. Debt finance is costly as monthly repayments must be made, while equity finance and retained earnings avoid costly monthly payments.
4. **Control** - Some types of finance can give away control of your company. For example, you may need to give premises as security for a loan. In the event that you can't pay back the loan, it will be sold by the bank to make the repayments. Different sources of finance could impact on ownership and control in a business. Issuing more shares could spread ownership and control to more people. Additional shareholders will have a say in the business and an entitlement to future dividends.
5. **Risk** - Not being able to pay back a loan that is secured on an asset means losing that asset. This may result in you losing your business.

#### WHAT ARE THE MAIN SOURCE OF FINANCE FOR A BE ENTERPRISE?

The following are some of the sources of finance available to a business. There were looked at further in chapter Management Finance

Short Term	Medium Term	Long Term
1. Trade Credit	1. Leasing	1. Equity Capital
2. Bank Overdraft	2. Hire Purchases	2. Grants
3. Accrued Expenses	3. Term Loan	3. Debentures
4. Factoring Debt		4. Sale and Lease back
5. Invoice Discounting		

**Challenges new business face getting Access to Finance:**

It can be very difficult for new businesses to raise finance and convince investors to invest in the new business. Having enough working capital - capital that is used for day to day running of the business (Current asset - Current liabilities) will be challenging. Entrepreneurs will need both short- and long-term sources of finance and may need to acquire finance through loan capital from financial institutions or try to convince investors to give them the finance they require.

**WHAT ARE THE MAIN PRODUCTION OPTIONS FOR A NEW ENTERPRISE**

There are 3 types of production. These include 1. Job Production, 2. Batch Production and 3. Mass Production. A business may decide to use all 3 types or to subcontract production to another company to produce the product

**1. Job Production**
**Job Production**

<sup>Def</sup> This means Producing a single product at a time usually customized to meet the needs of a particular customer. When that job is finished the next job starts. It is used for relatively expensive or highly skilled items (Birthday cakes)

2021 - Question 8 (A)  
2014 - Question 6 (A)  
2009 - Short Question 9

Advantages (Benefits)	Disadvantages (Drawbacks)
1. Easier to customized - are made to order	1. Employees need to be highly skilled
2. A problem making one product doesn't means disrupt production of others	2. Doesn't benefit from economic of scale - it's a very slow process
3. More employee involvement equals more job satisfaction	3. More expensive for customers -
	4. Higher wage bill - due to skilled employees



**Features of Job Production**

1. Job Production is a method of production where goods are made to order, goods are not made for stock, they are an unique product which are made to specification.
2. Labour is highly skilled due to the customised nature of the product.
3. The production process generally requires very advanced machinery and equipment.
4. Items are expensive because skilled craftsmen are used/quality raw materials are used/specifications can be changed, and are therefore quite expensive

**2. Batch Production**

**Batch Production** <sup>Def</sup> This involves manufacturing a limited number of identical goods at the same time, such as cakes, breads or books. Each stage of production will be completed in a batch before all goods are moved onto the next stage

Some small companies use a combination of Job and Mass production.

Advantages	Disadvantages
1. Worker do not need to be as skilled as job production	1. Requires more equipment
2. More efficient and less time wasting	2. Batch production requires more management skills (POC)
3. The average cost of production is less than job production	

**Factors to consider when changing from a production method -**

2018 - Question 5 (C)  
2014 Question 6 (A)

1. **One type of product only (mass produced standardised product)** - Being a leader in price only. Can the business survive on price leadership alone?
2. **Demand/Does the size of market exist?** - Has adequate market research been carried out to determine the size of the market? / Is the demand for that product sufficient?
3. **Can quality be maintained** - across a large numbers of goods?
4. **Capital investment** - required/necessary finance. Can sufficient capital be raised as it is expensive to set up production lines? /machine maintenance costs can be high.
5. **Staff working conditions** - Will key people leave due to more repetitive work?/less variety (boredom)/Semi-skilled to unskilled. Could there be redundancy issues?

6. **Will it be more difficult to change** - can the business adapt the product to meet changing needs of customer?/less flexibility when producing just one product.
7. **The amount of space available** - will more space be required for new machinery and stock?
8. **Impact on the brand name.** Will the change affect the reputation of the business? /status of the brand?
9. **Competition** - Large markets can have dominant firms in place/Can this business compete?

### 3. Mass Production

**Mass Production** <sup>Def</sup> This Is continuous production of large quantities of identical goods. It is very highly automated. For Example, Cornflakes, Pens, paperclips

Because of the long runs production usually remains the same for long periods. It is usually used by companies who needs to produce very large quantities for a large market.

Advantages	Disadvantages
1. Reducing cost and selling price	1. Heavy financial investments (keep machinery working)
	2. Breakdowns in one part of the assembly line can results in hold ups
	3. Staff moral can decline it the work is repetitive

#### Challenges new business face selecting an organisation structure.

The method of production that a business will select will be influence by Economies of scale, type of workers required (low skilled or high skilled), where will the finished goods be stored.

### WHAT IS SUBCONTRACTING/OUTSOURCING

**Outsourcing** <sup>Def</sup> This means finding a supplier to manufacture part of or the entire product for you.

The company does not produce the product themselves they outsource (Give it to) it to another company. The Price, quality standards and delivery dates are all agreed in advance. This means

that the entrepreneur can concentrate on other areas. For Example, Nike owns just one small factory - subcontract to Taiwan, South Korean

Advantages	Disadvantages
1. Simplifies management	1. Less control over quality
2. Cheaper to Subcontract	2. Sometimes it is more expensive
3. Extra production staff not needed	3. The subcontract may decide to become the competitor
4. Suit business with seasonal dips	

### WHAT IS FRANCHISING

#### Franchising

<sup>Def</sup> This is an agreement between a owner (franchisor) and another business (Franchisee) to rent an existing established business. For this the franchisee gets to use the franchisor name, logo and business ideas. In return for a fee and percentage of the profits. For example - Camile Thai

2021 - Short Question 3

Advantages	Disadvantages
1. It is a form of expansion which requires, <b>low capital investment by the franchisor</b> as the capital used to expand the business comes from franchisees..	1. Control is lost over the day-to-day management of the franchise businesses.
2. Franchising permits a <b>more rapid expansion</b> . By using the franchisees' capital, the franchisor is able to establish a large number of outlets in a short period of time. Rapid expansion can be achieved <b>without incurring the overheads and costs associated with opening company-owned restaurants</b> .	2. The reputation of the whole business could be affected by the actions of one franchisee /poor quality standards/staff problems

<p>3. An owner will be more attentive than a manager. This is the central point which makes franchising so attractive. <b>The franchisor can be assured that the person operating its restaurant will be "attending to business" as much as they would.</b> By franchising the business, the franchisor places the expansion of his/her business in the hands of <b>people who are motivated to make it work</b> and are therefore more likely to succeed.</p>	<p>3. A training programme for franchisees will be required. This will be expensive and time consuming.</p>
<p>4. Economies of scale exist. There is strength in numbers. The successful franchisor can <b>command deals with various suppliers.</b> Can control supplies to various franchisees. The cost savings can increase the franchisor's profits.</p>	<p>4. Franchisees will have to be monitored on a regular basis.</p>
<p>5. A franchise system <b>requires less management than a company owned chain of restaurants.</b> Hiring, motivating and retaining competent staffing are all functions handled by the franchisee, not the franchisor.</p>	
<p>6. Because there is a smaller capital investment required the <b>franchisor's profits are generated on a much lower capital investment even though the revenue from franchised</b> restaurants may be less than that received from</p>	

## WHAT IS A BUSINESS PLAN?

### Business Plan

**Def** This is a written document that shows the present position of a business. It sets out the business objectives (where it want to go) and strategies in how to get there -marketing, production, ownership.

2012 - Question 6 (C)  
2010 - Question 6 (B)  
2008 - Question 7 (A)

It sets out the following -

- |  |  |
|--|--|
| <ol style="list-style-type: none"> <li>1. Who is setting up the enterprise?</li> <li>2. How is it going to be produced or promoted?</li> <li>3. Where is the finance coming from?</li> </ol> | <ol style="list-style-type: none"> <li>4.. What is the product or service?</li> <li>5. Where is it going to be sold?</li> <li>6. How much profit it's expected to Generate?</li> </ol> |
|--|--|

## Important (Benefits) of a business plan

The business plan is important for 3 reasons. These are -

1. Short- and long-term plans - A business plan will set out both short term and long-term plans over a period of time. It identifies where the business what to go and how it will get there.
2. Is needed to raise finance - It is a vial document when a business is looking for finance form a financial institution. No financial institution will give a loan to a business if they can't see how they will be able to repay the loan. The business plan will sell the idea to investors and encourages them to invest.
3. Reduces risk and set targets - Targets are set in figures which are used as a benchmark where standards can be compared against. If these standards are not meet action can be implemented and put in place so they can be achieved

## Evaluation of the business Plan

In my opinion a business plan will enable the business to determine if it can be commercially viable. It may support the business when seeking source of finance form potential investors

### Uses of a Business Plan

A business plan is used for the following reasons -

1. To Inform - all involved with business where the business is going, and actions needed to get there.
2. To Monitor - measuring progress against targets set out in the plan.
3. To Provide - information to banks and government for loans and grant applications.

### What information does a business plan contain.

A good business plan should include the following pieces of information -

2017 - Question 5 (C)

1. Description of entrepreneur/ owners - Skills, experience and personal investment, details of directors, details of shareholders, legal structure
2. Market Description & analysis - Size competition and target market
3. Description of the product/service - USP
4. Production Plan - Premises and equipment required, production type and plan, labour skill and raw materials, type of production, Targets set to be achieved, lead time for delivery of raw materials.
5. Marketing Plan - Results from market research, describes the Marketing strategy and marketing mix.
6. Management Plan - how will the business be organized and controlled.
7. Financial Plan - Forecasted revenue and costs, Cashflow forecast, production budgets, projected profits, Premises, equipment and raw materials.
8. Sources of finance - It important the business shows realistic estimates.
9. Profitability forecast - Breakeven chart, cash-flow budget, estimate P & L and balance sheet.

Potential investors will want to be assured that the entrepreneurs have examined the financial side of the business before they invest.

**The importance of a business plan for stakeholders****Employees**

2017 - Question 5 (C)

Employees are interested in a business plan to confirm if the business is going to survive so they can have employment security. They may also be interested to see if the business is going to expand and possibly offer opportunities for promotion in the future.

**Investors**

Investors will be interested in a business plan to see if the business is capable of making a profit and offering a good return on their investment. Projected sales and market research results may persuade investors to provide capital to a business.

**Financial institutions (the cash position)**

Financial institutions require business plans from a business when they are seeking loan capital. It helps finance providers to make a decision regarding finance approval as they can see the experience of the owners/management and analyse their ideas. It is the primary tool to convey the potential viability of the business to finance providers.

**Management/employer**

Management will use a business plan as a source of control. They will use it to measure actual performance against goals and see if the business has progressed satisfactorily. The management have goals to be reached and the business plan provides benchmarks which they can use to monitor actual business performance against the set targets in the business plan.

**Suppliers**

Suppliers will be interested in a business plan of one of its customers to ensure that the business is viable and can sustain any line of credit that is offered to them. Government Agencies Government agencies will be interested if finance or other assistance is sought by businesses.

**ISSUE TO ADDRESS WHEN SETTING UP A NEW BUSIENSS.****1. Raising finance/capital**

The business will have to decide how much debt capital and equity capital she is going to use as sources of finance for the growth and expansion of her business. Debt capital carries the risks associated with being highly geared. Fixed interest repayments on debt capital must be made regardless of profitability.

2015 - Question 5 (C)  
2014 - Question 7 (C)  
2011 - Question 7 (A)

**2. The Production method**

A firm must choose an appropriate method of production that suits the type of good being manufactured and the potential demand for the product. Job or batch production have different demands in terms of automation, staffing and storage. Lia will have to opt for job or batch production in order to manufacture the different range of products she is selling.

**3. Ownership options**

An ownership structure has to be decided upon. Different structures have different demands in terms of risk, control, ownership, liability, tax implications. It would be advisable for a startup company to choose a private limited company structure because of the benefits of limited liability, incorporation and raising finance

**4. Marketing**

Being able to market the business conducting market research to identify if there is marker and demand for the product. How big is the market and producing a product to meet the consumer needs. They will also have to deciding on brand, the product USP to make it stand out from competitors and advertising the product.



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# Chapter 21

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## Getting Started

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### Unit 5

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### Higher Level

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### Past Questions (For this chapter)

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**SHORT QUESTIONS****2021 - Question 3**

Camile is a healthy, sustainable fast-casual restaurant franchise

- (i) Explain the term franchising


- (ii) Outline one benefit of a franchising as a start - up option


**2016 - Question 6**

Describe two features of job production

(i)
(ii)

**2009 - Question 9**

Contract 'job production' and 'batch production, giving one appropriate example in each case.


**LONG QUESTIONS****2021 - Question 8**

- (A) Discuss the three challenges below that a new business start-up must address
- |                     |            |         |      |
|---------------------|------------|---------|------|
| Ownership structure | Production | Finance | (20) |
|---------------------|------------|---------|------|

**2018 - Question 5**

- (C) Discuss the factors a business should consider before changing from a batch to a mass (flow) method of production (15)

**2017 - Question 5**

- (C) (i) Outline the main section contained in a business plan
- (ii) Explain the importance of a business plan for two different stakeholders (20)

**2015 - Question 5**

- (C) Read the information supplied and answer the question which follows.

Having been made redundant, Lia O'Brien has decided to set up her own enterprise manufacturing individually designed disposable tableware and paper cups for small coffee shops and restaurants. She recognises, however, that having an idea and having the will to succeed will not be enough to ensure success.

Discuss the key issues Lia will have to address before setting up her business enterprise. (15)

**2014 - Question 6**

(A) Read the information supplied and answer the questions which follow.

Sarah Fleming is a wedding dress designer and has worked for over 20 years in the bridal and clothing industry. She specialises in creating unique wedding dresses with an emphasis on personal service. Business is good and Sarah has applied for a bank loan of €10,000 to finance expansion.

- (i) Name the type of production process used by Sarah.
- (ii) Outline two challenges for Sarah of this type of production process.
- (iii) Discuss two implications for Sarah of changing to another type of production process. (25)

**2014 - Question 7**

(C) Discuss three challenges facing business start-ups (15)

**2012 - Question 6**

- (C)
- (i) Explain the term Business Plan
  - (ii) Evaluate the importance of a business plan to an innovative new technology business (20)

**2011 - Question 7**

(A) Discuss two possible challenges associated with starting a new business (10)

**2010 - Question 6**

Read the information supplied below and answer the questions which follow.

Marie Nolan is the owner of 'Marie's Pizzas' a successful pizza restaurant with a home-delivery service. Demand for take-aways has increased, as more people are eating at home due to the economic downturn. Marie is planning to expand her business through franchising and her accountant recommends that a business plan should be prepared before going ahead.

- (B) Outline two benefits to 'Marie's Pizzas' of preparing a business plan. (10)

**2008 - Question 7**

- (A) Outline the benefits for a new business of preparing a business plan (15)

**2006 - Question 6**

Paula and Thomas have recently returned to Ireland having worked with transnational companies for ten years. They wish to set up in business together in Ireland manufacturing a range of new organic breakfast cereals. Paula has particular expertise in production and finance and Thomas in marketing and human resources

- (A) Draft a business plan for this proposed new business using 5 headings, outlining the contents under each heading (40)