

Chapter 1: The Corporation

1.1 The Four Types of Firms

Comment: I think it is useful to think in terms of the relative advantages and disadvantages of each type of firm

A. Sole Proprietorships

=> business owned and run by one person

1. Advantage

=> easy to set up

2. Disadvantages

=> **owner has unlimited liability for firm's debts**

=> life of firm limited to life of owner

=> **difficult to transfer ownership**

B. Partnerships

=> like sole proprietorship except that more than one owner

1. Advantage

=> more than one owner

2. Disadvantages

=> **all general partners have unlimited liability for firm's debts**

Note: in limited partnership, limited partners have limited liability while general partners retain unlimited liability

=> partnership ends on death or withdrawal of any general partner

Note: does not end on death or withdrawal of limited partner

C. Limited Liability Companies

=> limited partnership with no general partner

1. Advantages

- => **all partners have limited liability and can manage firm**
- => company does not end with death of owners
- => profits passed on to owners untaxed at corporate level (not mentioned in text)

2. Disadvantages

- => earnings subject to self-employment tax (not mentioned in text)

D. Corporation

=> a legal person separate from its owners

1. Advantages

- => **owners have limited liability**
- => no limit on number of owners or who can own stock
- => easier separation of management and ownership of firm
- => **easier to raise capital**

2. Disadvantages

- => profits taxed twice (corporations pay tax on profits, owners pay tax on distributions from firm)
Note: "S" Corporations pass earnings on to owners without being taxed at corporate level (only at personal level of owners). Strict limitations on qualifications for S tax treatment (see text).
- => potential for conflict of interest between owners and managers

Q: What are advantages and disadvantages of organizing a business as a sole proprietorship, as a partnership, and as an LLC?

1.2 Ownership Versus Control of Corporations

=> *ask in class:*

Q: What is the role of a firm's board of directors? Why might a board of directors fail to fulfill its role?

Q: When should the government step in to protect society from a business?

- Q: What role do hostile takeovers play in resolving potential conflicts between the owners and managers of a firm?
- Q: Why are bankruptcy and liquidation of a firm separate decisions?

1.3 The Stock Market

Types of orders:

Limit order: submit an order in which specify price (and number of shares) at which willing to buy (bid) or sell (ask).

Market order: order in which specify number of shares want to trade at whatever price exists in the market now

=> if buying, pay the ask price (the lowest price at which anyone is willing to sell)

=> if selling, receive the bid price (the highest price that anyone is willing to pay).

Bid price: highest price anyone has posted at which willing to buy; price at which sell if submit a market order

Ask price: lowest price anyone has posted at which willing to sell; price at which buy if submit a market order

Youtube video: (posted by Faith Frank in Spring 2021 Canvas discussions): [Bid-ask Explained](#).

Ex. Look at prices for Apple on Yahoo Finance and CBOE exchange (when markets are open):

Summary page: <http://finance.yahoo.com/quote/aapl>

CBOE stock exchange:

http://markets.cboe.com/us/equities/market_statistics/book/AAPL/

Notes:

- 1) Yahoo summary page shows current bid and ask prices and number of shares available at each price
- 2) CBOE stock exchange shows range of bid and ask prices and number of shares at each price not just the best bid and ask price

Q: What price will you pay if you submit a market order to buy 100 shares of Apple?

Q: What price will you receive if you submit a market order to sell 100 shares of Apple?

Q: What happens if submit limit order to buy/sell 100 shares of Apple?

=> *ask in class:*

Q: What advantage does a stock market offer investors and corporations?

1.4 FinTech: Finance and Technology

Introduction to FinTech on Investopedia: <https://www.investopedia.com/terms/f/fintech.asp>

Note: the video near the beginning of the article gives a nice overview of FinTech.

Note: See the text for a discussion of each of the following topics:

- A. Telecommunications
- B. Security and Verification
- C. Automation of Banking Services
- D. Big Data and Machine Learning
- E. Competition