Answers to End-of-Chapter Review Questions

1. The four legal forms of business organization are proprietorships (businesses owned by single individuals or families, the businesses are the personal property of the proprietors), partnerships (businesses owned by a group of two or more individuals, the business does not exist apart from the people who own it, needs to be reconstituted if partners change), corporations (legal entities separate from the people who own them, individual owners can come and go, if a corporation goes bankrupt its debts are dissolved with it), and cooperatives (each owner has only one vote, normally run by hired managers, typically owned by workers, suppliers, or consumers).

2. The world’s largest corporations are primarily based in the United States, Western Europe, or Japan with a few located in Canada, Australia, and South Korea. The largest corporations have annual gross sales in excess of $160 billion. (Wal-Mart was the largest in 2002 with sales of $219 billion.)

3. The “stakeholder theory” of the corporation states that corporations are complex organizations that have responsibilities to many constituent “stakeholders,” such as shareholders, employees, neighbors, creditors, suppliers, customers, etc. The shareholder theory of the corporation states that corporations are merely legal instruments for carrying out the will of their shareholders.

4. Principal-agent theory discusses how one economic actor, the “principal,” can try to influence the actions of another, the “agent,” so that the principal’s objectives will be carried out.

5. The two main models of management are conflict (managers generally want workers to work harder and produce more, while workers want more control over the conditions and pace of work; work effort is motivated through close supervision, coercion, threats of demotion, job loss, etc.) and cooperation (productivity depends upon the effective interaction of many different people; workers must feel they have a stake in the long-run success of the firm).

6. The three kinds of “economies” that may make bigger operations more efficient are economies of scale (increasing production brings decreasing per-unit production costs), economies of scope (cost savings by making a wide range of products), and transactions cost economies (savings on the costs associated with market transactions, which may lead to organizing production within a single enterprise).

7. Some reasons why businesses may stay small include the potential for diseconomies of scale in some industries, franchises that allow for the benefits of small-scale ownership and management, the desire for some consumers to purchase goods and services from small-scale enterprises, and the dependence of some large firms on smaller firms.
8. Three ways in which businesses can be globalized are by owning and operating subsidiaries in more than one country (becoming a multinational corporation), by selling products or purchasing inputs in international markets, and by subcontracting and offshoring.