

FORMAL AND INFORMAL BUSINESS

Formal business

Refers to enterprises registered with the registrar of companies.

Characteristics of formal business

Registered business

Provide salaried employment

Proper record keeping

Governed by business laws/Acts of parliament

In most cases have corporate ownership of resources

Have employee and employers unions

Use recommended technology

Produce good quality products

Mostly urban based/sub urban based

Mostly use skilled labour

In most cases production is for commercial purposes

Advantages of Formal Business

Help an enterprise to be legally recognized. Since businesses are registered with the registrar of companies is legally recognized.

Lead to proper organization. Formal businesses are registered which makes them well organized.

It is easy to get bank loan; before a loan is got from financial institutions a business has to be legally known.

Enable businesses to be reliable and permanent. They cannot easily change location and purpose for formation as stated. It is to get skilled labour due to job security.

Gives a sound base for growth and development ; Before a business is registered, it has to have the required registered capital which gives basis for further development.

Comply with social security regulations. Registered businesses comply with all NSSF regulations in respect to employees.

Help one to benefit from government services when business is registered it's easy to get tenders, security, finances from government.

Provide a separate legal entity. Formal businesses have a separate legal entity different from owners.

Disadvantages of Formal Business

They are not easy to start; they need first to have all legal documents required for registration.

Enterprises are not flexible. Formal businesses inject in a lot of capital and register formation purpose. It is not easy to adapt to new changes in market.

They are governed by strict laws. The operation of formal enterprise depends on laws and regulations of the government.

Do not form basis for starting new industries to have a formal enterprises requires a lot; this discourages formation of micro enterprises.

Do not lead to fast employment generation. As formal businesses pay tax, it limits their capacity to create employment faster for citizens.

Informal businesses

Refers to enterprises that are not registered with register of companies

Characteristics of informal businesses

Mostly small-scale businesses

Mainly produce for the local market

Mostly use simple production techniques

Mostly produce consumer goods

Limited record keeping

Mainly sub-urban and rural based

Not registered

Dominated by solo proprietors

Most of them produce low quality goods

Most of them have low productivity

Mostly use unskilled and semi- skilled labour

Advantages of informal businesses

They are adoptable to change

They lead to fast employment

They are easy to start as they almost have no requirement

They form a basis of initiating new ideas

They earn higher profits as most requirements and taxes are dodged

They do not have a separate legal entity from their founders

Disadvantages of informal Businesses

They are not legally recognized

They are not properly organized

They are not reliable

They do not have clear access to loans from financial institutions

They do not comply with social security

They are closed by the government any time.

Strategy for Rural development

Most of small and medium enterprises are located in urban neglecting rural areas. The government has put in place strategy for rural development;

1. Rural development policy. Development of rural areas as urban dwellers depend on rural areas for supplies, majority of Uganda's population lives in rural areas.
2. Rural industrialization strategy. This aims at promoting SMEs in all regions of Uganda. It is for bringing industries and industrial employment to rural areas of Uganda.
3. Adoption for appropriate technology. It is for testing and approving new production techniques for rural areas, and assist farmers with the design and production of small scale farm equipment.
4. The spread of industries. It aims at helping entrepreneurs and produce products that cater for rural daily basic needs.

Constraints to Rural Development

Low level of education among rural entrepreneurs for effective development

Shortage of required tools and equipments for business operation

Lack of required skills in rural areas for starting and managing enterprises

Inadequate finance as most rural enterprises lack collateral to access loans

Poor infrastructure like roads, electricity, water that hinders industrial development.

Insurance for Small and Medium Enterprises

Insurance refers to where every person exposed to a risk pays a small amount of money to insure against the risks. Those who suffer the stated risk are compensated out of the pools

Principles /Doctrines of Insurance

- a. Insurable interest. This requires that before one insures property, he must have interest in it. He has to suffer in event of the risk insured taking place.
- b. Utmost good faith (Umberima fides). Requires one applying for insurance to disclose all material facts concerning property to be insured. This helps to accurately calculate premium to be paid. In case some facts are most disclosed and it is found out, the already paid medium is not refunded and policy cancelled.
- c. Subrogation. It states that after compensation has been made, the wreck/scrap should be taken by the insurer. No one should gain out of the loss.
- d. Indemnity. States that insurance does not benefit a person but restores him in the former financial position he was before the loss.
- e. Proximate cause. There must be a close relationship between the cause of a loss and the actual risk insured for compensation to be made.

Types of Insurance in Business

There are majorly two types of insurance.

1. Life insurance / assurance. This cover insurance of human life. It is in form ;
 - i. Whole life policy. Where compensation is paid death. Premiums are paid throughout the life of the insured.
 - ii. Endowment policy. Requires premium to be paid for a specified period and compensation is paid at death or expiry of the period whichever comes first.
 - iii. Life annuity/Annuities. Under this policy the insurance company arranges to pay fixed regular amounts during the life time of annuitment.
 - iv. Group life insurance. Under this families or business partners take out insurance to provide pension during old age.

- v. Sickness policy. This covers against specified diseases or all forms of all curable diseases. The insurer pays the medical bills of the insured and other expenses involved depending on the contract
2. Non-life or property or general insurance. This covers all belongings of the insured. It covers the insurable risks that would cause financial loss if people's property were destroyed.

Examples include;

- a. Fire insurance. This is taken to protect business against losses resulting from fire out breaks. Fire policy protects against fire damages and consequential losses due to fire out breaks.
- b. Theft and burglary. A businessman insures against losses due to theft and forced house breaking. This can be by employees or outside people
- c. Loss of profits. The entrepreneur insures against loss of profits in the trading periods up to an agreed percentage.
- d. Money at premises or in transit. An entrepreneur insures loss against money while leaving premises or at premises. Money kept At premises may be stolen causing loss of money.
- e. Motor insurance. Insures against motor vehicles loss due to theft, accident or fire. It includes:
 - i. Comprehensive. covers a range of risks
 - ii. Third party only covers other people hurt by the insured vehicle. It is compulsory to all vehicles in Uganda.
- f. Aviation insurance. It insures against loss resulting from personal accidents and large damages of aircraft crashes. The insurance company stands to compensate such losses.
- g. Marine insurance. This insures a water vessel and cargo transported on water. Marine cargo insures goods transported on water. Marine hull covers against loss of vessel damages towards third party and passengers.
- h. Machinery break down and consequential loss. It helps to cover the businessmen against machinery breakdown and other losses as a result of machine breakdown
- i. Employers' liability .An entrepreneur insures against losses suffered by employees while at work or during working hours.

Major term used in insurance

1. Insurer. Refers to the insurance company granting the insurance.
2. Insured. Refers to the person or business that takes out insurance and is promise compensation in the event of a loss.
3. Premium. This is the periodical contribution made by the insured to the insurer as a consideration for the insurance cover provided by the insurer. It forms a pool from which compensation is made to those who suffer loss.

Factors considered by the insurer when determining premium

- The nature of the property being insured. Delicate and fragile property/goods to handle e.g petrol stations attract higher premium than obvious goods.
- The number of people exposed to the same risk. The bigger the number the lower the premium because the cost spread than when the number is small.
- The frequency of the occurrence of the risk being insured. The higher the possibility of occurrence of the risk the higher the premium paid than were the possibility of occurrence is low.
- Operating expenses of the insurer. Higher administrative costs and rates claim of compensation attract higher premium than lower operating expenses.
- The desired profit margin of the insurer. If the insurer aims at making high profit then a high premium is charged than where the insurer aims at making sale maximization.
- Precautions taken by the insured to reduce the risk. Availability of precautions like fire extinguishers in buildings, safety belts in vehicles tend to reduce premium rates than were there are no premiums completely.
- Type of policy to be bought. Short term policies mostly attract less premium than long term policies.
- Value of the property to be insured. Expensive goods attract higher premium than cheap goods.
- Age of property. Old article and items face higher chances of damage hence attract higher premium than new articles.
- Level of income in case of life insurance. High income earners are charged higher premium as their beneficiaries have to be given higher compensation than low income earners.

Types of risks

- Insurable risks. These are risks whose probability of occurring can be statistically calculated from the past experience. E.g fire.
- Non-insurable risks. These are risks whose probability of occurring cannot be statistically calculated or determined. E.g fall in demand, war.
- Pure risk. These are risks that involve only a chance of loss.
- Speculative risks. These are risks which can give either a gain or loss.

Loss. Refers to the occurrence of the risk against which insurance is taken up.

Types of loss

- a. Total loss. Is when the entire property given has been destroyed.
- b. Partial loss. Is when part of the property insured has been destroyed

Other Terms Used Under Insurance

1. **Sum insured.** This is the value of the property insured as stated by the owner at the time of applying for insurance.

2. **Over insurance.** Is when the insured over declares value of his property at the time of insurance. She/he will be required to pay higher premium but at event of total loss he/she will be paid the correct value of the property.
3. **Under insurance.** This is where the insured under declares the value of his property at the time of insurance, is charged lower premium but in the event of total loss is paid only the sum insured.
4. **Contribution.** This occurs when different insurers raise funds in different proportions to cover a claim or expensive property co-insured with them.
5. **Co-insurance (Double insurance).** This is where the insured takes out an insurance policy for the same risk with more than one insurance company.
6. **Re-insurance.** This is when the insurance is so heavy or expensive that one insurer cannot cover it alone so it also insures part with another insurance company.
7. **Actuary.** This is a professional person who calculates premium rate basing on available statistics and information.
8. **Adjustor/ assessor.** This is a skilled person who calculates loss before compensation is made.
9. **Beneficiary.** This is a person entitled to receive compensation from a certain insurance policy.
10. **Insurance broker.** This is an expert in insurance business who transacts insurance business on behalf of an insurance policy.
11. **Insurance under-writer.** This is an individual who negotiates and enters into an insurance contract on his /her own behalf.
12. **Surrender value.** This is the money paid back to the insured when he or she decides to cancel the insurance cover before the period of specified or expiry.
13. **Settlement.** This is the payment agreed upon in case of total loss or occurrence of the risk.
14. **Proceeds.** This is the amount of money paid to the beneficiary as compensation.
15. **Liability.** This is the obligation of the insurer to compensate the insured when stated risk occurs.
16. **No claim bonus.** This is the discount offered to the insured that is not claimed for on the insurance policy. This reduces the amount of premium paid by the insured.
17. **Paid up policy.** This is where the insured requests the insurer to make arrangements that pays premium at once than making regular payments.
18. **Renewal.** Refers to giving a new life to an insurance contract.

Documents used in insurance

- i. **Proposal form.** This is an application form provided by the insurer requiring hi/ her details of property and risk to be insured. It signifies his willingness to pay the premium.

Contents of a proposal form

- a. The applicants name and address
- b. The occupation and location of the applicant
- c. The age of the applicant
- d. Name and the insurer
- e. The risk to be insured

- f. The policy to be bought
 - g. The sum insured
 - h. First insurance or last insurance
 - i. Any precautions taken against the risk
 - j. The signature of the applicant
 - k. The declaration of the applicant that the information disclosed is true.
 - l. Any other relevant facts about the property insured.
- ii. **Cover note.** It is a proof to show that premium has been paid to and accepted by the insured which undertakes to indemnify or compensate the insured. It is valid for 30 days during which the policy must be insured.
 - iii. **Claim form.** This is a document filled by the insured (claimant) to notify the insured that he/she has suffered the loss through the risk covered by the insure.
 - iv. **Insurance policy.** This is a document of contract between the insurer and the insured containing all conditions, major terms and warranties of the contract of the insurance.

Contents of an insurance policy

- a. Name and address of the insurer
- b. Name and address of the insured
- c. The property of the insured
- d. Period for which the policy is valid
- e. Amount of premium paid
- f. The value of the property insured/sum insured
- g. Terms and conditions for compensation
- h. The type of insurance policy under taken (risk insured against)

Importance of an insurance policy

- It holds the two parties to be responsible
- It serves an evidence of contract between the insurer and insured
- It acts as collateral security for the insured to acquire a loan
- It guarantees the continuity of a business in case of occurrence of a risk
- Enables the insured to be compensated in case of a loss
- It spells out terms and conditions of the contract

Steps involved in taking out an insurance policy

1. Acquiring quotations from different companies before deciding which company to insure with.
2. Choosing the insurance company to do business with.
3. Analyzing the budget and deciding how much money to pay for insurance
4. Filling in proposal form which acts as an application for insurance
5. Signing proposal form after making first payments of premium calculated

6. Regular payment of premium to the insurance company
7. Issuing an insurance policy which is an agreement between the insured and insurer

Terminating an insurance policy. This is the process of bringing an insurance contract between the insurer and insured to an end.

Circumstances under which an insurance policy may be terminated

- In case of distraction of the subject matter
- When the insured under or over declares
- In case of failure to pay premium
- If the insured insures a property in which he/ she has no insurable interest
- If the insured has been compensated
- If the contract has expired

Importance of insurance to business

1. Helps the individual in business to save money that is used to cover emergencies
2. Provides money to business that is used in different times
3. Provides businessmen with loan that are used to expand business
4. It provides employment chances to people as secretaries, managers hence source of startup capital etc
5. Helps to safe guard property of businessmen against risks like fire
6. It measures business company in operation as it gives compensation
7. Insurance companies act as trustees for the businessmen look after property of deceased and pay fees for the insured

Responsibilities of insurance companies for the business community

- Reduction of costs like workman's compensation, public limited policy
- Promoting trade (international trade) by insuring policy covering goods in transit
- Ensuring continuity of the business by giving compensation
- Safe guarding property of businessmen against all risks
- Acting as trustees for the business men by looking after the property of the deceased
- Enabling business people to save money that can be used to cover emergencies
- Compensation in case of loss
- Providing insurance policies which are used as collateral security to acquire loans

- Encouraging investment confidence in the business community
- Educating the business community like campaigns on safety and health care

Categories of insurance policies

Essential coverage

1. Fire insurance, cover damages due to fire, lighting and losses to goods moved temporary from your premises due to fire. If precautions have been taken to reduce the risk installation of fire extinguishers low premium is paid
2. Liability insurance, covers loss regarding customers, employees and any with whom you do business, one can take up umbrella policy covering premises and operations, owners and contract obligations, personal injury liability and others
3. Auto mobile insurance covers bodily injury liability, property damage liability ,medical payments insured motorists coverage and others

Desirable insurance coverage

1. Fire insurance extended insurance coverage. Covers wind storms, hail storms, riots, vehicles, damage on buildings, and vandalism in addition to basic fire policy.
2. Time element coverage. It ensures against income lost and expenses getting back into the business after the risk taking place. It includes business interruption insurance, rent insurance, accident and sickness.
3. Automobile added coverage. Covers creditor life, car turning and labour collusion and comprehensive coverage for fire, theft, flood, and damages to car.
4. Fidelity bonds. Protects employer against losses as a result of dishonest employees.
5. Store keeper's burglary and robbery coverage. It compensates losses that arise from bodily injury or forced entry. The losses compensated include robbery inside and outside premises, kidnapping, theft from residence, robbery of watchman and others.
6. Boiler and machinery. Covers damage to heating plant if it blows up, other damages caused by explosion, consequence

damage and occupancy payment if you are forced to move to other quarters.

7. Glass insurance. It covers damages to show window or doors. Premiums are based on the size, number of windows and their replacement costs.
8. Title insurance. It ensures legal work to secure a clear title.
9. Health insurance. It covers hospitalization of you and your employees and their dependants.
10. Life insurance. You buy life insurance for your own and that of your employees.

Challenges faced by insurance companies in Uganda

- Limited information about insurance among the business community
- Limited capital
- Urban concentration
- Limited skilled labor/ underwriters
- Insecurity in some parts of the country
- Laxarity of some clients who fail to use precautions e.g fire extinguishers, helmets
- Over or under declaration by clients
- Poor infrastructure to access all premises
- Corrupt employees
- Economic instability e.g inflation, fluctuating interest rates
- Limited markets/ stiff competition
- Misconception of insurance as being for the rich

Family and Business

In Uganda some businesses are family owned and other groups of people. Owning business as family requires good managerial skills, if it is to survive longer. However, most small enterprises depend on family labor to exist.

Factors that necessitate good relationship between family and business

1. Joint family funding; Family members' pool resources to start business. They have influence in decision making, employment policy and the type of

goods to produce. This makes it important to have a good relationship.

2. Inheritance; Business started by family are passed on from one generation to another. It is seen as an asset to the family.
3. Fear of hired management.
4. Source of employment to family members.
5. Managerial decision making.

Challenges Associated With Family Business

1. Challenge of decision making. There is difficulty in taking business decisions especially with finance some have personal interests that don't favour the business.
2. Challenge of succession of the business. In case of death, it is not easy to decide who is to take over the family business. This causes conflicts and affects business performance.
3. Limited skills to operate business. In most cases, family members employed don't have all required skills to effectively run business.
4. Challenges of finance. Money required to start and operate business may not be enough. This because family savings sometimes are not enough.
5. Limited information access. Business information about marketing, production, financial is not enough.
6. Laziness among family members.
7. Theft and misuse of family funds and stock.
8. Withdrawing of goods from the business for their personal/ private use
9. Taking the business for granted.
10. Challenge of compensating family members.
11. Role confusion as each member's responsibilities are not defined.
12. Limited managerial skills.
13. Centralized control system by family heads.
14. Conservatism of family members.
15. Challenge of communication due to role confusion.

16. High turnover of non family members.
17. Emotions due to family disagreements.
18. Informality as in most cases are not registered businesses.
19. Tunnel vision. Limited outside opinions and diversity on how to operate the business.

Solutions to the challenges of family business

1. There should be a clear ration are in hiring external professionals. Hired labour needs to concentrate on routine management and family members on policies and growth.
2. Roles and needs need to be spelt out clearly for family members in terms of authority rank.
3. There is need to register family business to have a separate legal entity. It needs to spell out authority relations and succession.
4. Family members who violate set procedure need to be disciplined and guided.
5. In case of disagreements it's necessary to invite expatriates to give technical advice on controversial issues.
6. Remuneration needs to reflect work done but also be in line with other enterprises.
7. Business contacts need to be kept at higher level – exchange of business information on various issues is important.

Ways through which family can support Entrepreneurs' business

- i. Giving financial support in terms of capital to enable an entrepreneur start and operate the business.
- ii. Assisting in the management of the business by helping in the execution of some of the business management tasks and functions as well as handling different activities in business operations.

- iii. Allowing the entrepreneur to use the assets of the family, e.g land , buildings, furniture, etc. to start and run the business.
- iv. Giving moral support to the entrepreneur.

Importance of family savings in establishing enterprises

1. It's most convenient as there are no interests paid or financial costs involved.
2. It helps in paying for a business license. This helps to get permission to operate business.
3. Helps in paying rent for business premises .in case family business does not have where to operate from; family savings are to hire premises.
4. It helps in buying business requirements savings are used to purchase tools machinery, equipment and furniture.
5. It's used to purchase stock. Family savings help to acquire raw material or finished goods and other factor inputs.
6. It allows to make own decisions. The entrepreneurs' plans and use money anytime.
7. Helps the family to be in complete control over the arising from business operations

