### Conceptual Framework Of Corporate Social Responsibility

#### 1. Conceptual Framework Of Corporate Social Responsibility

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1.1 **INTRODUCTION** :-

All human beings are in the boundary of social since they are society bounded who live in group. They cannot leave society, community by very nature they are social animals. They are to do some work of other for their living and then look for comforts. All human activities may be divided into economic and non-economic activities. Economic activities are designed to attain and use the material resources of life. Those economic activities half in the production of goods and services. Economic activities aim at proper allocation and optimum use of resources. The aim of all economic activities is to maximize the satisfaction or profit or welfare of the individuals. Since resources are limited and scare, individuals should use those scare resources at the best possible manner to achieve maximum satisfaction. Economic activities are undertaken to produce goods and services to satisfy human wants. The human efforts are directed for the welfare of society. All categories of works, occupations and professions are undertaken to create wealth and satisfy human needs.

**FISCHER** gives two objectives for economic activities.

- proper allocation of resources and
- Optimum use of resources

Economic activities may be classified into business, profession and employment. Business is a sum total of activities purpose with a purpose to produce and accumulate wealth. Business is an activities concerned with earning money

Objectives of business are categorized into

- Economic objectives
- Human objectives
- Social objectives
- Organic objectives
- National objectives

Thus, Social objectives of business are otherwise called ‘social responsibility of businesses.

According to **Brownin, H.R.**, social responsibility is defined as “obligation (of manager) to peruse those policies to make those lives of action which are desirable in tours of objectives and values of our society.”
In the words of STONIER “in real sense the assumption of social responsibilities implies recognition and understanding of the aspiration of the society and determination to contribution to its achievement”.

The responsibility of the business is to understand the needs and requirements of the society and thus direct its energies to fulfill them. Business should undertake anything which in favor of society. Business and society co-exist the business has two aspects such as:

- Individual and
- Social

Individual aspect deal with profit motive. Whereas social obligation is treated as social aspect. Business exists in society and is a part of society. The business should conform varies social needs. The social responsibility of business can be studied into:

I. Availability of goods
II. Supply of quality goods
III. Co-operation with the government
IV. Creation of more employment and
V. Utilizing national resources properly

Corporate social responsibility (CSR), also known as corporate responsibility, corporate citizenship, responsible business, sustainable responsible (SRB), or corporate social performance, 1

1.2 Concept of Social Responsibility

However, while doing so two things need to be noted to view it as social responsibility of business.

First, any such activity is not charity. It means that if any business donates some amount of money to any hospital or temple or school and college etc. it is not to be considered as discharge of social responsibility because charity does not imply fulfilling responsibility.

Secondly, any such activity should not be such that it is good for somebody and bad for others. Suppose a businessman makes a lot of money by smuggling or by cheating customers, and then runs a hospital to treat poor patients at low prices his actions cannot be socially justified. Social responsibility implies that a businessman should not do anything harmful to the society in course of his business activities.
“The obligation of any business to protect and serve public interest is known as social responsibility of business”

Thus, the concept of social responsibility discourages businessmen from adopting unfair means like black-marketing, hoarding, adulteration, tax evasion and cheating customers etc. to earn profit. Instead, it encourages them to earn profit through judicious management of the business, by providing better working and living conditions to its employees, providing better products, after sales-service, etc. to its customers and simultaneously to control pollution and conserve natural resources.

1.3 **MEANING OF SOCIAL RESPONSIBILITY**

The concept of social responsibility of business has its roots in the objective of the business itself. The objectives and responsibility are two side of the same coin of business. This is now realized by almost all businessmen all over the world. The industrialists and businessmen have now accepted that they owe a responsibility to the society at large.

According to **OLINER SHELDON**, a British business leader, founded on:

I. Awaking of the social environments
II. Awaking of public interest in the inner workings of business
III. Demand of the workers for more leisure time and increased opportunity for self-development
IV. A trade union or group of workers or political clubs are interested in working of companies around it.
V. Problem – solving by the management to obtain a proper balances between production and human areas.²

The contemporary view of social responsibility of business is substantially broader and benevolent them the classical one.

➢ **CLASSICAL AND CONTEMPORARY VIEWS:**

The contemporary view of social responsibility of business is substantially broader and benevolent then the classical one.

According to the classical view, business has only economic objectives and no other responsibility beyond that.

**MILTON FREEDMAN**, a noble economist and a proponent of this view, argues that “there is one and only one social responsibility of business to use its
resource and engage in activities designed to increase if profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud few found could so thoroughly undermine the very foundation of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible. This is a fundamentally subversive doctrine”

According to STEINER, a reasonable approach to social responsibility is as follows.  

1. Each business must take into account the situation in which it finds itself in meeting stockholder expectations.
2. Business is an economic entity and cannot loopy its profitability meeting social needs.
3. Business should recognize that in the long run, the general social goods everyone.
4. The social responsibility expected of a business is directly related to its social power to influence outcomes.
5. Social responsibility is related to the size of the company and to the industry it is in
6. A business should take only social problems in which it has competences.
7. Business must assume share of the social Burdon and be willing to absurd reasonable social costs.

The article of business leaders on corporate social responsibility

“Here are the obscurations of some business leaders speaking at a summit on, corporate social responsibility (CSR).

According to N.R.Narayana Murthy, chairman and chief executive officer of Infosys technologies, corporate fore most social responsibility is to create maximum share holder value working under the circumstances where it is fair to all its stake holders – workers, consumers, the community and environment. He points out that by living in harmony with the community and environment around us and not cheating our customers and worker’s we might not gain anything in the short-run, but in the long term it means greater profits and shareholder value.
In the opinion of Aman Mehta, CBO, HSBC, Hongkong, however, it is not so straight forward. Aman Mehta says that CSR as a concept is different to different people in different countries. Fundamentally, CSR is balancing the afflicted info rest put on the corporation from different stockholders with the objectives a commercial organization in such a way that there is minimum loss to anybody.

**Bertrand collamb**, chairman and chief executive officer, Lafarge, France, observes that a company can’t be successful in the long-run without a happy community around and a motivated and happy workforce with would translate into greater labor productivity, lower wastage in manufacturing process and product rejection rate resulting to him international companion can exhibit a greater social responsibility by bring in efficient manufacturing and business practices to the developing countries and training and educating local people in new skill, and knowledge”.

**Social responsibility is a nebulous idea and hence is defined in various ways.**-

“Adelphi burley has defined social responsibility as the manager’s responsiveness to public consensus. This means that there cannot be the same set of social responsibilities applicable to all countries in all times.”

“**According to KEITH DAVIS**, the farm” social responsibility “refers to two types of business obligation viz.

1. The socio-economic obligation and
2. The socio-human obligation.”

### 1.4 **Need of Social Responsibility**

Social Responsibility of business needed to foster society and other integral parts of a nation.

They are:

1. To meet social needs;
2. Government is insufficient to need the social needs. So private business should serve society through its deployment of funds for welfare of society.
3. Besides Government, business entities provide social responsibilities to society.
4. Public pressure on business to serve society and community.
5) Environment pollution reduction.
6) Public demand;
7) Equal employment to all races;
8) Women’s liberation
9) Regulating Agencies.8

Social responsibility of business refers to what the business does, over and above the stator requirement, for the benefit of the society. The word responsibility cannot that the business has some moral obligation to the society.

Term corporate citizenship is also commonly used to refer to the moral obligation of business to the society. This implies that just as individual, corporate are also integral part of the society and that their behavior shall be guided by certain social norms.

**Article of Social Expectations**

“In the development of corporate ethics, sachar committee have reached a stage where the question of the social responsibility of business to the community. Can no longer be scoffed at or taken lightly. In the environment of modern economic development, the corporate sector no longer functions in isolation. If the flow if the company that they are performing a social purpose in the development of the company is to be accepted, it can only be judged by the companies. The company must have and function as a responsible member of society, like any other individual. It cannot shun moral value, nor can it longer actual compulsions. The real need is for the part of the management which is not limited to shares holders’ alien. In modern times, the objectives of business have to be the proper utilization of resources for the benefit of others. A profit is still a necessary part of the total picture, but it is not the primary purpose. This implies that the claims of various interest alone but from the point of view of what is best for the community at large. The company must accept its obligation to be socially responsible and to work for the large benefit of the community.”9

The operations of business enterprises affect a wide spectrum. The resources they make use of are not limited to those of the proprietors and the impact of their operations is felt also by many people who are in no way connected with the enterprises. The shareholders, the suppliers of resources, the consumers, the local community and society at large are affected by the way an enterprise functions. Hence
a business enterprise has be socially very responsive so that a social balance may be struck between the opposing interests of those groups.

**Goyder argues:**

“Industry in the twentieth century can no longer be regarded as a private arrangement for enriching share holders. It has become a joint enterprise in which workers, management and trade union officials all play a part. If the system which owner know by the name private enterprise is to continue, some way must be found to embrace many interests which go to make up industry in a common purpose.”

Later, in 1978, while delivering the C.C. Desai memorial lecture, he reiterated his plea that if the corporation has to function affectively, it has to be accountable to the public at large and he sought to equate the suggestion of a responsible company with the trusteeship concept advocates but Gandhiji, the aim of which was to ensure that private property was used for the common goods. The declaration issued by the international seminar on the social responsibility of business as

“Responsibility to customer’s workers share holders and the community”

**H.S SIGHANIA** classifies two nature of the social responsibility of business into two categories.

1) The manner in which a business carries out its own business activity.
2) The welfare activity that it takes upon itself as additional function.

The first involves the acceptance of the fact that business is not merely a profit-making occupation but a social function which involves certain duties, and requires that appropriate ethics are followed.

**For example:**

A business must obey all the laws, even when owners are disagreeable; it should produce the maximum goods of good quality, ensure smooth supplies at competitive prices, pay tacos, shun malpractices, and pay a fair wage to shareholders. It is also the duty of a business to undertake new investments and promotes the disposal of economic activity through ancillaryisation and the setting up of industries in backward area so as to spread enterprise and take employment to the doorsteps of labor. In addition to its commercial activity business also plays a role in promoting social welfare activity, even directly.”

Social responsibility is a voluntary effort on the part of business to take various steps to satisfy the expectation of the different interest groups. As you have
already learnt, the interest groups may be owners, investors, employees, consumers, government and society or community. But the question arises, why the business should come forward and be responsible towards these interest groups. Let us consider the following points:

I. **PUBLIC IMAGE** –

The activities of business towards the welfare of the society earn goodwill and reputation for the business. The earnings of business also depend upon the public image of its activities. People prefer to buy products of a company that engages itself in various social welfare programmes. Again, good public image also attracts honest and competent employees to work with such employers.

II. **GOVERNMENT REGULATION** –

To avoid government regulations businessmen should discharge their duties voluntarily. For example, if any business firm pollutes the environment it will naturally come under strict government regulation, which may Ultimately force the firm to close down its business. Instead, the business firm should engage itself in maintaining a pollution free environment.

III. **SURVIVAL AND GROWTH** –

Every business is a part of the society. So for its survival and growth, support from the society is very much essential. Business utilizes the available resources like power, water, land, roads, etc. of the society. So it should be the responsibility of every business to spend a part of its profit for the welfare of the society.

IV. **EMPLOYEE SATISFACTION** –

Besides getting good salary and working in a healthy atmosphere, employees also expect other facilities like proper accommodation, transportation, education and training. The employers should try to fulfill all the expectation of the employees because employee satisfaction is directly related to productivity and it is also required for the long-term prosperity of the organization. For example, if business spends money on training of the employees, it will have more efficient people to work and thus, earn more profit.

V. **CONSUMER AWARENESS** –

Now-a-days consumers have become very conscious about their rights. They protest against the supply of inferior and harmful products by forming different
groups. This has made it obligatory for the business to protect the interest of the consumers by providing quality products at the most competitive price.”

1.5. Features of Social Responsibility

- Welfare of society
- Values of society
- Aspiration of society
- It goods beyond the loan of the country
  - Social responsibility has significant in flounce on the social system.
  - Obligations and duties that business owns to society.
  - Business is no longer considered a tripartite venture i.e. owners, workers, and consumers but it has become a multiparty system and
  - Business is part of society and community and therefore it has to solve society in many ways.

Corporations are socially responsible for following:

A] Core consensus:

1) Obeying major laws.
2) Human treatment of employees.
3) Honest, truthful and fair dealing with other enterprises, consumers and employees.
4) Truthful financial reporting.
5) Providing reasonable quality and quantity of product or services for the price negotiated by parties.
6) Providing a fair return on investment to shareholders through profits.
7) Equal employment opportunity for entry level jobs.

B] Majority agreement among most industry groups:

I. Internal accounting capital expenditure budgets for major expenditures, including those for social benefits.
II. Obeying lows, for example, restricting pollution or unsafe practices. And products, establishing minimum wages and so on.
DIAGRAM-1.1

SOCIAL RESPONSIBILITY

- Internal Obligation
  - Share Holder
    - Due to justice, equity and morality in employee’s or finding & promotion
    - Employees’ Morale
    - Productivity
  - Government
  - Tax Collecting Authorizes
- External Obligation
  - Creditors Or Investors
  - Community
  - Suppliers
  - Management

(Source: Corporate Social Accounting and Reporting pg.26)
Table 1.1.

Responsibility of business towards society.

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<td>1] equity shares holders (owners)</td>
<td>Fair and adequate Crete of return. Steady capital appreciation to the share holders for their investments regular and up-to-date information about works of the company. Maximum disclosure about progress and achievement of the company. It must ensure planned growth, solvency and optimum utilization of the resources.</td>
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| 2] Employees | - Higher wages  
- Security of job.  
- Full employment  
- Bottom working conditions  
- opportunities for self development and promotion  
- social security  
- Welfares  
- Grievance settlement process  
- shoring of excess profits |
| 3] Consumers | - Quality goods and services at reasonable prices.  
- Regular supply of high quality products and services to consumers.  
- Managers must meet the needs. Of the consumers of different classes, tastes and with different purchasing power of the right time, place, price and in right quality.  
- Business has to protect consumers invest at any cost.  
- Honest advertisement right weigh of goods  
- Business must more carefully and efficiently. |
- promote human development between business and |
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| 5] Suppliers | - Fairness and truthfulness in all activities including pricing, licensing to sell and right to sell.  
- Ensure business activities are free from litigation.  
- Development term stability in the supplier relationship.  
- Pay suppliers on time their dues.  
- Supply information on reasonable times. |
| 6] Investors | - Disclosure of all information’s after the affairs of the company.  
- Conservation of assets by way of protection  
- Respect investor’s requests, suggestions etc.  
- Timely payment of all dues of investors applies professional management to maximize efficiency. |
| 7] Competitors: | - Faster and develop open marks for free trade and investments.  
- Promote healthy competitive behavior.  
- Respects to both tangible and intellectual property rights.  
- Faster ethical means and methods in business.  
- Maintain healthy competition. |
| 8] Nation: | - Use property the nation scare resources  
- About pollution  
- Pay taxes on times  
- Proper assessment and right payment of taxes.  
- Abiding the laws and respecting the acts.  
- Environmental protection.  
- Respect to community and citizen of the country. |
9] Complete truth less in adverting.
10] Harmless products and services
11] Harmless production processes to local committees in which they are situated.
12] Employee benefits that assure. Family health, security and welfare during, at least, person’s employment.

13] Contribution to local charitable causes in cash or kind or both.
14] Equal employment Opportunities to all committees and both boxes.
15] Recording and reporting social responsibility actions.

C] Minority agreement among
16] Equal employment opportunities to various rules, at all levels, sexes regardless of difficulty and costs.
17] Improving the local environment by reducing pollution.
18] Improving quality of life of employees, consumers and local residents by all means.
19] Actively pursuing improved social concerning customers, suppliers, loser’s ad other groups that are affected directly by the company.
20] Measuring recording and publishing detailed descriptions of social benefits and costs and social assets and liabilities on a regular basis in the annual financial reports.

Levels: Three levels of corporate social responsibility
Level I: “Business has the responsibility to make a profit while dealing fairly and honestly.”
Level II: “Business has a responsibility to society with respect to its employees and products, and a responsibility to mirror the ideals and values of the society within its own microcosm.”
Level III:
“It is a primary obligation of business to use its power to promote social and perceived as moral.” 14

1.6  Social Orientations of Business

“The extent of social orientations of companies varies very widely. Further the social orientation or the extent of social involvement of a company may change over time.
SOCIAL RESPONSIBILITY MODELS:

There are some models which endeavor to describe the evolution an extant of social orientation of companies notables ones include Carroll’s models hatel’s model and Ackermann’s model.

“ARCHIE B. CARROL, who defines corporate social responsibility as the entire range of obligations business has to society, has proposed a three dimensional conceptual model of corporate performance.

According to CARROLL, a firm has the following four categories of obligations of corporate performance”

- Economic
- Legal
- Ethical
- Discretionary

The firm being an economic unity its primary responsibility is economic, i.e. efficient operations to society economic needs of the society and generation of surplus for reworking the investors and further development. Legal responsibilities are also fundamental in nature because a company is bound to obey the law of the land.

Ethical responsibilities are certain norms which the society expects the business to observe. Through they are not mandated by low. For example, a company shall not resort to bribing or unethical practices, unfair competitive practices etc.”

“Carroll later presented the different categories of responsibilities as a pyramid of corporate social responsibility.

According to CARROLL’S pyramid, legal responsibilities come only at the second stage. This is not a right view. Company must inevitably obey the laws, even if it is unable to discharge some of the economic objective as long as it exists.”
“WILLIAM. E. HALAS’s return –on- resources model of corporate performance.” 17 recognizes the fact that no corporate social posture will be value-free, and this makes corporate social responsiveness a tremendously difficult task. This calls for tradeoffs which involve both economic and ethical decisions that will not necessarily satisfy the needs of every staunch older.

According to ACKERMAN’S MODEL, There are three phases in the development of the social responsiveness of a company.

I. The top management recognized the existence of a social problem which deserves the company’s attention and acknowledges the company’s policy towards the company’s it by making an oral or written statement.

II. The second phase is characterized by the company appointing staff specialists or external consultants to study the problem and suggest way of dealing with it.

III. The third phase in values the implication of the social responsibility programmers.
1.7 **Social Responsibility of Corporate Sector Towards Different Groups**

**Diagram:** 1.3.

**Climates of social responsibility of corporate sector**

![Diagram of corporate social responsibility]

**Analysis of Above Diagram is as under:-**

“There is no unanimity of opinion as to what constitutes social responsibility of business. The important generally accepted responsibilities of the business to different sections of the society are described below:

**7.1.1. Responsibility to Shareholder**

The responsibility of a company to its shareholders, who are the owner, is indeed a primary business one. The that the shareholders have taken a great risk in making investment in the business should be adequately recognized.

To protect the interests of shareholders and employees,” **the primary business of a business is to stay in business**”. To safeguard the capital of the shareholders and to provide a reasonable divided the company has to strengthen and consolidate its position. Hence, it should develop and improve its business and build up its financial independence.
Needless to say, to provide divided, the company should earn sufficient profit. Adequate reserve should be build up so that it will be able to declare a reasonable divided during a lean period as well.

If a company fails to cope with change in a changing and dynamic world, its position will be shaken, and the shareholders’ interests will be affected. By innovation and growth the company should consolidate and improve its position and help strengthen the share prices.

The shareholders are interested not only in the protection of their investment and the return on it but also in the image of the company. It shall, therefore be the endeavor of the company to ensure that its public image is such that the shareholders can feel proud of their company.

**7.1.2. Responsibility To Employees**

The success of an organization depends to very large extend on the morale of employees and their whole – hearted co-operation. Employee’s morale depends to a large extent on the discharge of the company’s responsibilities to them and the employee - employee relationship. The responsibility of the organization to the workers includes:

- The payment of wages;
- The provision of the best working conditions;
- The establishment of fair work standards and norms.
- The provision of labor welfare facilities to the extent possible.
- Arrangement for proper training and education of the workers.
- Reasonable chances and proper system for accomplishment and promotion;
- Proper recognition, appreciation and encouragement of special skills and capabilities of the workers;
- The installation of an efficient grievance handling system;
- An opportunity for participating in managerial decisions to the extent desirable.

The committee that conducted the social audit of **Tata Iron and Steel Company** (TISCO) observe that “not only should the company carry out its various obligation to the employees as well as the large community as a matter of principle, but this has also led to the a higher degree of efficiency in TISCO works and an
unparalleled performance in industrial peace and considerable team spirit and discipline which have all resulted in high productivity and utilization of capacity”.

Thus, by discharging its responsibility to the employees, the business advances its own interests.

7.1.3. Responsibility To Consumers

According to PETER DRUCKER, “There is only one valid definition of business purpose; to create a customer.” Drucker observes: “The customer is the foundation of a business and keeps it in existence. He alone gives employment. To supply the wants and needs of consume, society entrusts wealth-producing resources to the business enterprise”.

It has been widely recognized that customer satisfaction shall be the key to satisfying the organization goals. Important responsibilities of the business to the customers are:

I. To improve the efficiency of the functioning of the business so as to (a) increase productivity and reduce prices
   (b) Improve quality, and
   (c) Smoothen the distribution system to make goods easily available.

II. To do research and development, to improve quality and introduce better and new products.

III. To take appropriate steps to remove the imperfections in the distribution system, including black-marketing or profiteering by middlemen or anti-social element.

IV. To supply goods at reasonable prices even when seller’s market is.

V. To provide the required after-sales services.

VI. To ensure that product supplied has no adverse effect on the consumer.

VII. To provide sufficient information about the products, including their adverse effects, risks, and care to be taken while using the products.

VIII. To avoid misleading the customers by improper advertisements or otherwise.

IX. To provide an opportunity for being heard and to redress genuine grievances.

X. To understand customer needs and to take necessary measures to satisfy their needs.
7.1.4. Responsibility to the Community

A business has a lot of responsibility to the community around its location and to the society at large. There responsibilities include:

1) Taking appropriate steps to prevent environmental pollution and to preserve the ecological balance.
2) Rehabilitating population displaced by the operation of the, if any.
3) Assisting in the overall development of the locality.
4) Taking steps to conserve scarce resources and developing alternatives, wherever possible.
5) Improving the efficiency of the business operation.
6) Contributing to research and development.
7) Development of backward.
8) Promotion of ancillarisation and small-scale industries.
9) Making possible contribution to furthering social causes like the promotion of education and population control.
10) Contribution to the national effort to build up a better society.

1.7.5 Responsibility Towards Investors

Investors are those who provide finance by way of investment in debentures, bonds, deposits etc. Banks, financial institutions, and investing public are all included in this category. The responsibilities of business towards its investors are:

- Ensuring safety of their investment,
- Regular payment of interest,
- Timely repayment of principal amount.

1.7.6 Responsibility towards Suppliers

Suppliers are businessmen who supply raw materials and other items required by manufacturers and traders. Certain suppliers, called distributors, supply finished products to the consumers. The responsibilities of business towards these suppliers are:

- Giving regular orders for purchase of goods.
- Dealing on fair terms and conditions.
- Availing reasonable credit period.
Timely payment of dues.

1.7.7. **Responsibility towards Competitors**

Competitors are the other businessmen or organizations involved in a similar type of business. Existence of competition helps the business in becoming more dynamic and innovative so as to make itself better than its competitors. It also sometimes encourages the business to indulge in negative activities like resorting to unfair trade practices. The responsibilities of Businesses towards its competitors are:

- Not to offer exceptionally high sales commission to distributors, agents etc.
- Not to offer to customers heavy discounts and/or free products in every sale.
- Not to defame competitors through false or ambiguous advertisements.

1.7.8. **Responsibility towards Government**

Business activities are governed by the rules and regulations framed by the government. The various responsibilities of business towards government are:

- Setting up units as per guidelines of government
- Payment of fees, duties and taxes regularly as well as honestly.
- Not to indulge in monopolistic and restrictive trade practices.
- Conforming to pollution control norms set up by government.
- Not to indulge in corruption through bribing and other unlawful activities. 

1.8 **Uses of Social Responsibility**

“The uses of social responsibility of business towards society are:

I. To give a clear picture of the whole business entity on the social responsibility aspect;

II. To make better understanding of social activities of entity on various segments such as employees, management, stakeholders, consumers, suppliers, law markets, government, public and community;

III. To protect environment;
IV. To optimum use of national resources:
V. To welfare of employees;
VI. To protect the assets of business;
VII. To see welfare of community;
VIII. To respect the laws of the land;
IX. Prosperity of community;
X. Development of economy of a nation;
XI. Improves the standard of living;
XII. Fair price of goods to consumers;
XIII. Fair and healthy competition;
XIV. Social justice; protection of rights of workers and
XV. Quality control;”

1.9 **Social Responsibility In India**

Business and Society are interdependent. Society depends on business for meeting its needs and welfare, whereas, Business depends on society for its existence and growth.

**Corporate Social Responsibility** is an ethical or ideological theory; a doctrine, how an entity whether it is a government, corporation, organization or individuals has a responsibility to society and can be defined as, “the obligation of business to pursue those policies, to make those decisions or to follow those lines of actions which are desirable in terms of the objectives and values of your society”.

As rightly said, “It is better to be proactive towards a problem rather than reactive to a problem. One part of Social Responsibility is being responsible to people, for the actions of people and for actions that affect people”, hence it means obligation of business towards different social group, i.e. the consumers, employees, shareholders, society, government, media and so on. As Abraham Lincoln once said that public sentiments is everything. With public sentiments nothing can fail, without it, nothing can succeed.

In 2001, Kaliski believed, “In today’s society a business must maintain ethical principles in order to be successful. Business can use ethical decision leading to strength their business in three main ways. The 1st way is to use their ethical decision
making to increase productivity of the employees, the 2nd way to strengthen their business is by making ethical decisions towards their stakeholders that are outside of the business environment, via customers and suppliers and the 3rd way that business can use ethical decision making to secure their business is by making decisions that allows the government agencies to minimize their involvement with the corporation.

**The utilitarian principle says** – Act in a way that results in the greatest goods for the greatest number. The Social Responsibility Concept is beneficial to the Business and the Society. “The most significant contribution organized industry can make is by identifying itself with the life and the problems of the people, of the community to which it belongs, and by applying its resources, skills and talents to serve and help them”- Late J. R. D. Tata.

Thus, every business must have a code of conduct as a guideline which directs human behavior and helps to them differentiate between good and bad, right and wrong, fair and unfair, professional and unprofessional as well as determining universal rules and laws of a behavior. It can be seen within the company in various departments like Human Resource Management (recruitment, selection, induction, training, promotion, payroll, retention and motivation); Marketing Management (sales, distribution, advertising, promotion, public relation, publicity); Finance (auditing, risk management, taxation, cost analysis); Production(logistics, warehousing, supply chain, quality control), thus it is an inseparable management activity function.

Social Responsibility is voluntary, it is about going above and beyond what is called for by the legal responsibility; it cannot be imposed by law, thus, it needs willing acceptance and self discipline. As the golden rule says, “Act in a way you would want others to act toward you.”

According to Renowned Indian Jurist NANI PALKIVALA, “What is the point in having laws and laws upon laws if your inner consciousness is not there, which enables you to do right things for a right conclusion. In other words; if you are to looking for fairness and justice all around it has to be found within the heart of the businessmen. If the ethical sense dies in the heart of the businessmen, no constitutions, no law, no court can save it. It is only within yourself that you have to
find the ideals you are struggling to establish. Finally, the famous words of Earnest Dale, “It is the duty of business to provide fair returns to the shareholders, fair working conditions to the employees, fair deal to the suppliers and customers to make the business an asset to the local community and nation.

CSR is not new to India; companies like TATA and BIRLA have been imbibing the case for social good in their operations for decades long before CSR become a popular cause. In spite of having such life size successful examples, CSR in India is in a very nascent stage. It is still one of the least understood initiatives in the Indian development sector. It is followed by a handful of public companies as dictated by the very basis of their existence, and by a few private companies, with international shareholding as this is the practice followed by them in their respective foreign country. Thus the situation is far from perfect as the emphasis is not on social good but rather on a policy that needs to be implemented.

A lack of understanding, inadequately trained personnel, non availability of authentic data and specific information on the kinds of CSR activities, coverage, policy etc. further adds to the reach and effectiveness of CSR programmers’. But the situation is changing and CSR is coming out of the purview of ‘doing social good’ and is fast becoming a ‘business necessity’. The ‘business case’ for CSR is gaining ground and corporate houses are realizing that ‘what is good for workers - their community, health, and environment is also good for the business’.  

Forerunners in corporate social responsibility:

“Today's buzzword, Corporate Social Responsibility or CSR has been part of the Tata Group ever since the days of Jamshetji Tata. Even while he was busy setting up textile ventures, he always thought of his workers' welfare and requirements of the country. From granting scholarships for further studies abroad in 1892 to supporting Gandhiji's campaign for racial equality in South Africa to giving the country its first science centre, hospital and atomic research centre to providing relief and rehabilitation to natural disaster affected places - they have done it all.

Jamshed Irani, Director, Tata Sons Ltd, says, "The Tata credo is that 'give back to the people what you have earned from them'. So from the very inception, Jamshetji Tata and his family have been following this principle." Moreover 'he says that for any business to sustain in the long run they have to look beyond business.
Ages ago when Corporate Social Responsibility was either the government, or charitable organizations headache, the Tata’s aggressively worked for the upliftment of the community. Tata initiated various labour welfare laws, like the establishment of Welfare Department was introduced in 1917 and enforced by law in 1948 or Maternity Benefit was introduced in 1928 and enforced by law in 1946. While today eyebrows are being raised about corporate doing social work, the Tata Group feels it is the need of the hour. Thus, where in the West companies are doubtful of spending the shareholders money and corporates”.

1.11. CONCLUSION

Thus, the obligation of any business to protect and serve public interest is known as social responsibility of business.

Corporate sector play important roll towards shareholders, employees, consumers, community, investors, suppliers, competitors, and government.

Corporate social responsibilities towards shareholders are interested not only in the protection of their investment and the return on it but also in the image of the company. Responsibility to employees the success of corporate sector depends to very large extend on the morale of employees and their whole – hearted co-operation. Consumer is the foundation of a business and keeps it in existence therefore corporate sector responsible for it for it, increase productivity and reduce prices, improve quality, and smoothen the distribution system to make goods easily available. Corporate sector responsible for community to prevent environment pollution, contribute to research and development, development of backward. It is responsible for investors to ensuring safety of their investment, regular payment of interest, timely repayment of principal amount. Responsible for suppliers to give regular orders for purchase of goods, deal on fair terms and conditions, available reasonable credit period, timely payment of dues. And also responsible towards government not to offer exceptionally high sales commission to distributers, agents etc., not to offer to customers heavy discounts and or free products in every sale, not to defame competitors through false or ambiguous advertisements.

Social values may indicate good and desirable business conduct in the best interest of society. Business is created by society anticipating it would aid society. Society expects a lot of responsibilities and obligations. Although profit earning is essential for the survival of entity, it would spend certain amount of its earnings for
the betterment of society and of business entity and decision makers to take actions which protect and improve the welfare of the society as a whole along with their own interest. The scope of social responsibility reporting includes:

1. Net income contribution;
2. Human resources contribution;
3. Public contribution;
4. Product or service contribution.

The term contribution includes both benefits and costs associated with an organization’s activities.

Hence, corporate sector play important intermediate social corporate responsibility towards different groups.
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1.1 **INTRODUCTION**

“Accounting is a language of business. Accounting is an analysis and interpretation of accounting records containing financial and economic information of transactions and other events profitably to a business. To operate a business profitably and to stay solvent, profitability and solvency of a firm should be measured at regular intervals in order to know the aggregate position since alarming is the art of measuring, describing and interpreting financial and economic activities of a business, it is essential, for an accounting system, to record, classify and summaries the entire. Lot of events since accounting is a language of business, it should be communication to the parties related to and integrated in its activities. Such communication is made through corporate reporting process. It has assumed goat significances in recent years. In many countries the users of such reports. There are many parties who are much interested such as equity shareholders, lenders, bankers, financial institutions, tax-levying authorities, regulating authorities, government and various authorities in the accounting reporting of companies. By statutes, all the companies and corporate entities are reporting minimum information mandatorily”.¹

Adam Smith in his famous book ‘Wealth of nations’ stated that “Economics is an enquiry into the nature and cause of wealth of nations”.²

“Value added is a basic and important measurement to judge the performance of an enterprise. It indicates the manufacturer during a specific period of time. No enterprises can survive and grow, if it fails to generate wealth. An enterprise may exist without profit, but cannot survive without adding value. Value added is meaningful measure of corporate performance than conventional measures based on traditional financial accounting and can be particularly useful for employee’s oriented approach, which will allow more fruitful discussion with employees and can be especially useful in productivity arrangements. The value added is a basic and broad standard comprises investment by shareholders, debentureholders, creditors and specialized financial institutions. If such investment not create wealth (value addition), it means that is misuse of public funds. Therefore the concept of value added has a direct linkage with the concept of the business. Value added can be particularly useful to management in comparing the performance with its industry as a whole. Financial reporting has traditionally concentrated on the needs of
shareholders and creditors but value added statement is important for stakeholders as well as employees point of view.”

“A business organization is an independent, separately identified doing business to earn profit and serve society with quality goods at reasonable prices. The profit or loss of business is related with various agents such as shareholders, money lenders, government, customers, suppliers, creditors, debenture holders, financial institutions, banks, tax collecting authorities, employees and many others.”

“The fundamental objective of corporate reports is to communicate economic measurement and information. About the resources and performances of the reporting entity useful to those having reasonable rights to such information”.

Contribution of a business enterprise cannot be evaluated by the profit and loss account. So, there is a need for improving the understandability of the traditional accounting system shown in the corporate reporting. Now-a-days the concept of profit maximization has losing its significance and all the firms are moving towards the concept of wealth maximization. After introducing Economic policy in 1991 new Multi-national Companies attract towards Indian economy, which has compelled the company managements to look after the all concerned factors which help them in smooth operation of the company. Published annual reports and accounts are the major tools for company management, with which they provide the full information regarding their Company’s business operations, results future prospects etc. The published annual reports have established its great impotence not only among the share–holders but also all other groups who take interest in the company. So it has become necessary for the company management to provide all information relating to financial statements in its annual reports and accounts. Value added statement is one of the statements which require having its place in annual reports now a day. The Value Added statement has been prepared for measuring the ‘Wealth Created ‘by an enterprise.

“The basic motive behind conducting any business or trade is to maximize profit or wealth. It has been noted that businessman started to earn profit by fair or foul means. This results into exploitation and unfair practices. However with the change of time it is being realized that the main motive of business or human activities should be directed towards social welfare. Therefore the main motto of
business should be to add social value. Value addition is the social utility created by a concern by it’s a portions in the raw materials used to produce the product”.7

1.2 THE CONCEPT OF VALUE ADDED

The origin of the concept of value-added may be traced back to the year 1975 when the Accounting Standard Steering Committee in United Kingdom stressed and the inclusion of Value Added Statement in the corporate annual report. The real interest in presenting the value-added statement in the annual report has increased since the publication of the “Corporate Report”, a discussion paper issued by Accounting Standing Steering Committee8.

“Value added concept is comparatively new but is gaining considerable importance those days, particularly for taxation and managerial performance purposes. A growing number of companies in India have started including a value added statement (VAS) on the lines of the companies in western countries, as a part of their published annual reports and accounts. The concept of value added or wealth creation is a performance measure and it reports the wealth generated by a business undertaking over a period of time.”9

Accounting to the Institute of Charted Account of India. (ICAI), the term value added refers to “the increase in value of a product or service resulting from an alteration in the form, location or availability excluding the cost of brought out materials and services.”10

“There are basically two concepts of value added as given below.

I. The Economic concept of Value – Added.
II. Accounting concept of Value – Added.”11

I. The Economic concept of Value – Added.

Value added in the views of economists is related with income. As such, the term ‘income’ is discussed first to explain a base for understanding the term ‘value added’. There is no unanimity amongst economists regarding the concept of income. Most of the economic associates it with national income. National income is the value
of final goods and services produced during a specified time period within the national boundary.

Accounting to National Income Committee, a national income estimate measures the volume of commodities and services turned out during a given period counted without duplication.¹²

In this, concepts, both volumes of goods as well as services produced are equally treated as income. This practice is universally accepted by the social scientists and the idea is accepted in measuring social income by all the countries. Expect the socialist countries, who follow the views of Karl Mark.¹³ The social approach do not treat services as part of income and accordingly, adopts ‘physiocrats’ concept in measurement of national income however, the economists are divided into two groups, On group known as the pronouncers of the comprehensive production concept, includes both production of goods produced and services rendered in measuring the social income. While the other group known as the socialist group, includes only goods produced in measuring the social income.

The concept of comprehensive production to be more justified and used by most of the economists. Thus, the value of goods produced and services rendered is treated as income.

According to Dudley Dillard, “The gross national income or product s the money value services produced during a given period, and the not national income is squall to the gross national income minus depreciation and obsolescence of capital assets”¹⁴

The sale proceed of the goods produced and services rendered is distributed among various factors of production employed in generating the products and services in the form of wages to the labour, rent to the land, interest to the capital and profit to the entrepreneur. So, alternatively, GNP (Gross National Product) can be calculated by aggregating all incomes corned by different factors of production. As mentioned by Paul Wannacott and Ronald Wamacott, “the national income is the sum of all income derived by firm from the factors of production. It included wages, Salaries, Rent, Interest and Profit” ¹⁵
In order to eliminate the drawback of double counting a third method of measuring national income was developed with is popularly known as the ‘value added method’. This method is based on the fundamental assumption that no production unit can create products without seeking help from its previous producer starting from the nature’s gift in a chain. Production units either natural goods or goods obtained from other producers as raw material and with the help of labour used on them with the agency of instruments produce. Thus, each production unit adds value to the existing value of goods and services obtained from other units.

However, use of labour, capital and management efforts on natural or required products on natural or required products generates utilities having market values. So each entity is said to obtain from other commits entities

The amount of value added is shared by different factors of production of the society in the form of wages, rant, interest, profit etc. the amount of original services purchased by each entity equals the value added by that entity, since it is the value of the services of factors of production that additional value.

However, the added value is created by efforts of the entity and its employees and is equal to the market value of the goods produced less cost of brought in goods and serviced from outsides. These methods of measuring value added do not includes the contributions of other firms to the total value of production of the firm. So that it is essentially equal to the market value created by the entity.

In shape of mathematical formula, it can be presented as follows.

\[ V_a = V_t - V_R \]

Where,

\[ V_a = \text{Value Added} \]
\[ V_t = \text{Value transferred to the units} \]
\[ (\text{I.e. sales value}) \]
\[ V_R = \text{Value Received from other units as input} \]
The basic idea behind the above concept is that income would be said to emerge. If the sales value exceeds the cost of bought in goods, even though cost of labour, services obtained, capital etc. may not be fully recovered. In other words, value added income is said to be generated, the moment VT-VR is positive. The economists are interested to know this perception of income represented by VA that is, the amount of production, (not sales) and how this production is shared among the owners of land, labour capital and entrepreneurship.20

Thus, it may be concluded that according to economic concept of value added, it is addition in the GNP during a specified time span the figure of added value is shared by different members of society hence it increases social welfare.

II) Accounting Concept of Value Added.

Value added is the surplus of sales revenue plus other incomes from goods and services over the cost of bought in goods and services from outside. As stated in the glossary issued by the Institute of chartered accountants of India, that value added is “The increase in market value resulting from an alteration in the form, location or availability of a product or service excluding the cost of bought in materials and services.”21

Ruggles is of the view that, “the value added by a firm i.e. the value created by the activities of the firm and its employees alone, can be measured by the differences between the market value of the goods that have been turned out by the firm and the cost of those goods and materials purchased from other firm.”22

Annual survey of Industries (ASI) described value added as that part of the value of the product which is created in the factory and is computed by deducting from the gross ex-factory value of output, the gross value of input.”23

The terms ‘the gross ex-factory value of output’ and ‘the gross value of input’ correspond with those of ‘the market value of goods that have been turned out’ and ‘the cost of those goods and materials purchased from other firm’ respectively. Thus, in accounting value added is the excess of ‘output’ over ‘input’. For better understanding the terms ‘output’ and ‘input’ are described in detail.
Output:

Output includes goods processed during a specified time period (irrespective of being sold or remain unsold in the stock) and services sold. It includes excess of closing semi-finished products over opening semi-finished products and time and place utility created by the firm in case the goods are sold at the same condition as those were purchased.

Input:

Input includes materials consumed and purchased of non industrial services which carry charges like postage, audit fee, legal fee, gas and electricity etc. ensured material i.e. material remaining in stock at the end of period are not considered as input.

Salaries, wages, bonus etc. paid or payable to employees and also interest and rent are not considered as input.

“Value added represents the total wealth generated by the effects of all providers of capital plus employees and the government. It can be obtained by the following rearrangement of the income statement:

\[ S - B = W + I + DP + E + T \]  \hspace{1cm} (I)

\[ S - B - DP = W + I + E + T \]  \hspace{1cm} (II)

Where,  

- \( E \) = Earning,
- \( S \) = Sales Revenue,
- \( B \) = Purchases of Material & Services,
- \( W \) = Wages
- \( I \) = Interest
- \( T \) = Taxes
- \( DP \) = Depreciation.

Equation (I) express the gross value added;
Equation (II) Express the not value added.

In both equations, the left side (the subtractive) shows the value-added (Gross or not) and the right side (the additive side) shows the disposal value among the stock holders.

Equation (II) can also be arranged as follows:

\[ S - B - CDP = E + (W + I + T) \] \[ \text{OR} \]
\[ NVA = E + NE \]

Where,

\[ NVA = S - B - DP = \text{Not value – added and} \]
\[ NE = W + I + T = \text{Non – earning components of not value added} \] 24


According to R. G. Sharma, “Value Added is a basil and important measurement to judge the performance of an enterprise” 26.

The concept of value added is direct linkage with the concept of social responsibility. Added value is a form of wealth but there is not natural wealth like land, buildings, minerals, etc. Added value is a measure of wealth generated by the collective efforts of people who woke in the industry. Value added is a form of wealth but all forms of wealth are not value added.

According to S. Gupta, ‘Value added means excess of turnover plus income from services over the cost of goods and services’ 27.

Value added amount computed by deducting from sales revenue plus income from services, the cost of bought-in-materials and services excluding depreciation is termed as “Gross Value Added” (NVA).

The added value concept has got many uses. Economists have uses the VA concept for long in a ‘Macro’ sense. The G.N.P. is calculated as under: -

\[ \text{G.N.P} = \text{Wages} + \text{Rent} + \text{Interest} + \text{Profit} \] 28.
Economists also explained what Value Added is the sum of all expenditure of the community distinguishing between expenditure on consumption and expenditure on investment. Accountants have defined the value-added concept in a different way. They considered that, “Value added is the wealth the company has been able to create by its employee’s efforts during a period”\(^{29}\).

The value added concept emphasis that the performance of the enterprise. Represents the collective efforts of employees, management and providers of capital. The value-added concept also aligns corporate financial reporting with “National Income Accounting”\(^{30}\).

Value added is included in the computation of G.D.P. But one thing must be kept in mind that everything has got to be done within the limitations set by the accepted accounting principles and conventions. There principles and conventions, it may be mentioned here, are founded on certain basic assumptions like continuity, accrual, consistency, conservatism, materiality and relevance. Although value added information is provided on a supplementary basis, it can not violate the established criteria of identification, measurement and reporting of accountable events and phenomena.

1.3 MEANING & DEFINITIONS OF VALUE-ADDED:

Value Added is the excess of sales revenue plus income from other sources over the cost of bought in goods and services purchased from external parties of enterprise. Some of the definitions of Value Added are given by different authors are as under.

**Accounting to Brech E. F. L** “the added value for a firm, or for any other organization, is the Value- Added to materials by the process of production. It also includes the gross margin of any merchant or factored goods sold”\(^{31}\).

“Value added indicates the ‘value’, ‘wealth’ or utility created by an enterprise during a specified period of time. Value added concept has been introduced for measuring the ‘wealth created’ by an entity. Value added is a form of wealth, but not all the forms of wealth add to the value. Items like, minerals, metals, coal, oil, timber, water, air, land and similar sorts of wealth are by nature”. \(^{32}\)
According to **E.S.Wood**, “Value added is the kind of wealth that is generated by efforts and ingenuity of manking”.

**Lewis and Pendrill** mentioned that, “Value added may be calculated as the difference between the value of good or services produced by the team, i.e. sales revenues, less the value of goods and services purchased from outsiders, i.e. the cost of bought in materials and services.”

**John Sizer** is of the view that value added is the wealth the company has been able to create by its own and its employees efforts during a period.

**John Sizer** further explained and started that, “It is out of the value added cage that a company rewards its various stock holders, i.e. share holders, directors, managers, employees, in hand revenue etc.”

**Roger Brayant** “Clearly mentioned that “value added is the wealth the reporting entity has been able to create by its own and its employee efforts. This statement would show how value added has been used to pay these contributes to its creation.”

**Kohler’s Dictionary for Accountants** stated that “Value added is that part of the cost of a manufacture of semi-manufactured product attributable to work performed on constituent raw material.”

The publication of “The corporate report” in the year 1975, there were three concepts of value added, those are-

- Economic value added
- Accounting value added
- Market value added.

**According to brown J.L. & Howard L.R** “Sales value less the cost of bought in goods and services used in producing those sales.”

**According to Merely M.F.** “Value Added is the value which entity has added in a period equals it sales less bought in goods and services.”

**According to Wood E.G.** “Value Added measures the wealth created by a business or an industry.”
According to I.C.M.A. terminology “The increase in the market value resulting from an alteration in the form, location or availability of a product or service excluding the cost of bought – out materials or services”\(^42\).

1.4 **VALUE ADDED REPORTING**

Accounting procedure: Incase of value added reporting accounting procedure will be divided in two parts:

1). **Generation of Value Added** and,

2). **Application of Value Added**.

1. **GENERATION OF VALUE ADDED**

Value addition is the increases in the market value brought by an alteration in the form, location and availability of a product or services, excluding the cost of brought in material or services used in the that product or services. In simple words the value added is an excess of turnover + income from services over the cost of brought in material and cost of the services. Here turnover indicates (Gross sales +sales Tax and duties - (rebate + returns - (-commission + discount + Goods used for self consumption)). Income from services includes incomes in the form of dividend, rent, commission and other income. The word cost of brought in material includes purchases of material and consumed during the year, adjustment of WIP and finished goods The term cost of services represents the cost of services paid to the external parties for using the facilities given by them .The employees costs, excise duty and depreciation have not been included in the cost of brought in materials and services. There are certain non-value added items appear on the debit and credit side of profit and loss accounts, e.g. profit and loss on sale of investment and fixed assets, provision for bad debts, provision for taxation, on operating exp.( donations) these items . Should carefully be treated

Here,- Va means Value addition, \(VA=S+I-C\), \(S\) means sales, \(I\) means Income from Services and, \(C\) Cost of brought in material and services.\(^43\)

As the definition given by I.C.M.A, the “Value added is an excess of turnover plus income from services over the cost of bought in materials and cost of services”. The term ‘turnover’ includes the gross sales of goods plus duties and sales
tax, minus the amount of sales returns, goods used for self consumption, commission and rebates as well as discount allowed. The term ‘Income From Services’ includes in the form of dividends from subsidiary companies, insurance claims, rents, compensations and other miscellaneous income less scrap etc. The word ‘Cost of Bought – In Materials Consumed’ includes the cost of raw material consumed, trading goods purchase, the cost of packing materials, store and spares consumed. The amount should be again adjusted for the summation of work – in progress and finished goods. The term ‘Cost of Services’ includes the cost of services paid for external agencies for using the facilities offered by them. The items like employee’s costs, excise duty and depreciation have not been included in the cost of bought – in materials and depreciation has not been included in the cost of bought – in materials and services. There are some ‘Non – Value Added’ items appear on the debit and credit side of profit and loss account. The items are shown in the following chart. 

**Diagram-1.4**

- **Non Value Added Items**
  - **Non Value Added Items on Debit Side**
    - Loss on Sale of assets.
    - Provisions.
    - Written on Preliminary Expenses.
    - Charity, Donations.
    - Subscription of New Paper, Periodicals, Etc.
  - **Non value added Items on Credit side**
    - Interest and Dividend.
    - Rent and Sale of Scrape.
    - Profit on Sale of Asset.
    - Prior Years’ Charges.
    - Provisions Written Back.
    - Insurance Claim.
    - Miscellaneous Income.
2. APPLICATION OF VALUE ADDED

The amount of value added is mainly distributed among four major contributors like employees, government, provider of capital and the owner, if any excess remaining after the distribution, this will reinvested business for future development.

1. **Distribution of value added to employee:-**

   Employees are one of the major claimants of the value added. The employees include workers and all type of the staff. The items like wages and salaries, Managing Director’s Remuneration, Directors sitting fees, contribution to provident Fund, Staff welfare Expenses, etc. are included.

2. **Distribution of value Added to Government:-**

   The Central and State Government provides not only the infrastructural facilities but also conditions. The taxes and duties like customs duty, excise duty, sales tax, income tax, wealth tax, rates and taxes, etc. are included here. The amount of subsidizing on export should be deducted from the Government’s share.

3. **Distribution of Value Added to Providers of Capitals:-**

   Financial institutions are also gets Value Added in the form of interest. This includes interest on bank loan, interest on term loans, interest on debentures, dividends, etc.

4. **Distribution of Value Added to Owners:-**

   Share holders who are the owners of the organization provide Equity Share Capital to the business unit. All payments made to them such as interim dividend,
Conceptual Framework Of Value Added Reporting-B

Chapter-1

final dividend, bonus share are included under this heading. The balance of value added, if any should be shown separately under the heading of Retained Earning or ploughed back of profit.

Diagram-1.5

Above Diagram describe Generation of Value added and Application of Value Added.
1.5 METHODS OF CALCULATING V.A:

There are many different methods of calculating Value Added given different authors. Some of them are given below.

1. Method given by ICMA:-

The ICMA defined Value added as, “The increase in the market value resulting from an alteration in the form, location or availability can be explained with the help of following equation.

\[
\text{Value Added} = \text{Value after alteration} - \text{Value before alteration}
\]

2. Method given by Kohler:-

The concept of Value added defined by Kohler as, “That part of the cost of a manufacture or semi-manufactured product attributable to work performed on constituent raw material. This can be understood with the help of following equation.

\[
\text{Value Added} = (\text{Value of Out Put} + \text{Income Other Sources}) - (\text{Cost of Materials and Services Purchased form outside})
\]

3. Method Suggested by ASSC:-

The Accounting Standard Steering Committee (ASSC) suggests following formula for computation of Value added. The equation is as under.

\[
\text{Value Added} = a - b
\]

OR

\[
\text{Value Added} = c + d + e + f
\]

Where,

\[a=\text{Turnover}\]

\[b=\text{Bought in Materials and Services}\]

\[c=\text{Dividend and Interest Payable}\]
4. Some Other Methods of Calculating Value Added\textsuperscript{46}.

There are some other methods of calculating Value Added. They are as under.

- \textbf{Value Added} = Sales (net of excise duty) – Cost of throughput (items bought from outside and processed)
- \textbf{Value Added} = Profit + All Conversion and Other Costs.
- \textbf{Value Added} = Value of Production – Cost of Materials, Power etc.

1.6 MEANING OF VALUE ADDED STATEMENT:

According to the \textbf{Institute of Charted Accounts of India}, “Value added statement reveals that the value added by an enterprise. Which it has been able to generate and its distribution among those. Contributing to its generation is known as stock holders.” \textsuperscript{47}

Value added statement is a periodic statement and gives us an idea about the value created by the enterprise. During this period and as to how such value is distributed among the various parties contribution to such value creation. Basically every organization obtains certain input factors and inputs of goods and services purchased by the business for carrying out its activity.

\textbf{Value Added} = \textit{Money value of output} – \textit{Money value of inputs and services}

The publication of this statement along with corporate report was recommended by the \textbf{Accounting Standards Steering Committee} (ASSC) a publication corporate report published in 1975. This committee is now known as the accounting standards committee (ASC). The publication of this statement in India is not mandatory but many progressive firms give this statement in their published accounts. In U.K. it to mandatory for large firms to publish this report\textsuperscript{48}.
David Pen drill defines it as “the statement which shows the income of the company as an entity and how that is divided between this people who have contributed to its creation.”

1.7 Assumptions of the Preparation of VAS:

1. VAS is a substitute but a supplement to the profit and loss account:
2. VAS is based on items and figures obtained in the profit and loss account and the according concept remain the same in the preparation of VAS;
3. It is different from profit and loss account to the extent, the letter contains the non-valued added debits and credits like provisions, non-trading losses, appropriations as well as non trading incomes like profit on sale of scrap, interest on securities, dividend etc.

1.8 Features of Value Added Statement:

1) Performance Measurement:

VAS depicts the performance of an organization value added has been strongly advanced as performances measurement of an enterprise. This concept helps to measure capital productivity and not output of an enterprise.

2) Reporting:

VAS is superior over other forms of reporting, it tolls better about quality of reporting to various groups of parties attached to the concern.

3) Accounting Concepts:

Various accounting concepts, conventions and principle are followed while altering different elements or components of the value added statement. Various concept such as going concern, realization, revenue recognition, dual aspect, money measurement, etc. are adopted while preparing value added statement.

4) Background information and Data:

VAS provides information regarding generation and disposal of value added; it is no substitute but a supplement to the profit and loss account.
5) Inter related position Statement:

VAS can be regarded as an inter – related position statement as it depicts the relationship between value added and value distributed to parties outside the business, namely to employees, government, creditors and shareholders.

6) Wealth generation and disposal:

Value added statement shows how the wealth is generation in the business and who are the recipients of the wealth VIZ. employees, investor’s vendors, governments, tax collecting authorities and related earnings.

7) Reduced ownership Emphasis:

Company’s position is well explained thought value added statement which provides a mean to reduce the ownership compasses. This is not possible through the profit statement. The wealth has been distributed by the organization amongst those who have contributed to its creation.

1.9 Uses of Value Added Statement:

“Value Added” income data will aid government agencies in planning for the future by providing then with current information on the output of goods and services being provided by the enterprise and on input – output relations of the enterprise system.

A. Measurement of Output:-

i) Basis of National Accounting


iii) Measuring productivity of manpower and capital.

The value added concept can be used as a method of measuring output of a business, industry or a nation. Value added is the basis of national accounting.

VA is a measuring technique of measuring business performance.

It is measuring the productivity of manpower and capital. Value added, a measurement of output, is more useful than other measures such as physical
quantities, sales turn over, or profit although does not replaced than. It supplements then, rather.

B. Communication:

i) Explaining what business in about
ii) Presenting accounting information
iii) Basis for employee participation

Value added statement is explaining what business is about.

It is presenting accounting information about the business, both insiders and outsiders. Value added statement can be used for internal management for planning, budgeting, controlling decision – making purposes, besides, value added reports are used to aid out sides of the organization such as:

i) Share holders
ii) Customers
iii) Creditors
iv) Debenture holders
v) Suppliers
vi) Auditors
vii) Government tax-collecting authorities
viii) Researchers

Value added statement is used as a basic of employee participation VAS helps. To measure man power productivity in terms of value added per employee within the firm comparison of value added per employee can be made over successive months or years.

C. Rewarding Employees:

i) Basis for wage and salary policy
ii) Basic for group bonus schemes.

Value added is a basis for ways and salary policy. The index of value added per employee is a vital figure why because it sets a limit to the average wage per employee. No concern can pay out more in wages for employee than it is generating
in value added for employee unless it is subsidies. Concerns use added value as the basis for group bonus schemes for employee benefits.

D. **Business policy:-**

1) Marketing strategy
2) Capital investment policy
3) Business ratios

1) **Marketing strategy:**

Where a concern produces more than one product for sale, it needs market strategy. Usually, the ratio of added value to sales revenue varies from one product to another. More important the ratio of value added to the limiting factors of production, *e.g.* man hours or machine hours, various from one product to another.

A main objective of market strategy should be to generate more value added by dividing better products and better markets.51

2) **Investment Policy:**

“For calculation treating labour as a factor of production, a cost to be minimized. In such a situation value added technique is adopted for capital expenditure decision for generation of income instead of envontional measure by taking profit as a key measuring tool” 52

3) **Business ratio:**

“Value added provides a novel group of business ratios relevant to all parties like shareholders, creditor, customers, suppliers, debenture holders, government, taxing authorities and research organization added value ratios are significant for both employees and investors. The broad concept of value added presents a wider prospective and describing performance.”53

E. **Productivity :-**

A number of productivity measures can be devised with the value added statement, 54 for instance,
i) Value added for rupees of capital employed;
ii) Value added per rupees of sales;
iii) Value added per rupee of labour cost;
iv) Value added per employee;
v) Value added per labour hour; and
vi) Value added per machine hour.

1.11 METHODS OF PREPARING VAS:-

The business unit that does not make profit is deemed to be ill but the enterprise that does not add value is regarded as evil. This shows the importance of Value Added for a business unit. The Value Added is mainly a re-arrangement of information contained in the Income Statement. It also represents the Value Added by the company during a specific period of time and the way in which it is distributed amongst the various factor employees, government and providers of capital. There are mainly two methods of preparing Value Added Statement. They are given under in the form of chart.

Diagram-1.6

(Sources: Value Added Reporting – In Theory and Practices & Research By Mohana Rao)
Value Added Statement can be prepared in two divisions’ viz., Generation of Value Added and Application of Value Added. This Statement can be prepared as Gross Value Added (GVA) and Net Value Added (NVA). The GVA has two sub methods viz., Additive Method and Subtractive Method. The NVA also has two sub methods viz. Income Distribution Method and Net Output Method. The brief discussion about these methods is as under.

(A) Gross Value Added:-

B. Cox has suggested two methods for preparing Gross Value Added Statement.

(1) Additive Method:-

The Additive Method is a one part of preparing Gross Value Added Statement. This method is also known as Income Approach. This method can be represented in the form of equation as under.

\[
\text{Gross Value Added (GVA) = Profit before Tax (PBT) + Employees Cost (EC) + Depreciation (D) + Interest (I)}
\]

Symbolically, it can be written as:

\[
\text{GVA} = \text{PBT} + \text{EC} + \text{D} + \text{I}
\]

(2) Subtractive Method :-

The Subtracting Method is another method of preparing Gross Value Added Statement. This Method is also known as Product Approach. The equation of this method is as under.

\[
\text{Gross Value Added (GVA) = Sales (S) + Income from Services (IS) - Cost of Bought in Goods and Services (CBGS).}
\]

(B) Net Value Added :-

This method has suggested by Studneski Paul. He suggested two methods for calculation of Net Value Added. They are as under.
(1) Income Distribution method:-

This is one of the methods of preparing Net Value Added Statement suggested by Studneski Paul. The equation of this method is as under.

\[
\text{Net Value Added (NVA)} = \\
\text{Value Added to Employees (VAE) + Value Added to Government (VAG) + Value Added to Financier (VAF) + Value Added to Entity (VAE)}
\]

Symbolically it can be written as:

\[
\text{NVA} = \text{VAE} + \text{VAG} + \text{VAF} + \text{VAE}
\]

(2) Net Output Method:-

This is another method of preparing Net Value Added Statement. The equation of Out Put Method is as under.

\[
\text{Net Value Added (NVA)} = \\
\text{Gross Value Added (GVA) - Depreciation (D)}
\]

OR

\[
\text{Net Value Added (NVA)} = \\
\text{Sales Revenue (SR) - Cost of Bought in Materials and Services (CBMS) - Depreciation (D)}
\]

Symbolically it can be written as under.

\[
\text{NVA} = \text{GVA} - \text{D}
\]

OR

\[
\text{NVA} = \text{SR} - \text{CBMS} - \text{D}
\]

1.12 Objectives of VAS:-

The objectives of preparing Value Added Statement are as follows.
1. The fundamental objective of Value Added Statement is to disclose the value added by a firm during a period of time.

2. Value Added Statement indicates the Wealth Created by a business enterprise which is used as a tool for evaluating the performance of business unit.

3. Value Added Statement helps to study the pattern of distribution of Value Added to four contributors, viz. Employees, Lenders, Governments and Owners.

4. Value Added Statement helps Government to collect more revenue by way of levying tax on Value Added instead of net profit.

1.13 **Format of Value Added Statement:**

   Generally, value added statement is divided into two parts:

   - Application of value added
   - Distribution of value added

   According to the **Institute of Charted Accountants of India**, “Value Added Statement reveals that the Value Added by an enterprise which it has able to generate and its distribution among those contributing to its generation are known as stakeholders.”

Value Added Statement can be prepared in three forms which are shown as follows:

1. General Form
2. Report Form
3. Account Form

1. **General Format of Value Added Statement**

   A typical statement of Value Added is prepared as a part of management information system. The Value Added Statement is nothing but the re-arrangement of information presented in the Profit &Loss account. Nevertheless, the re-arrangement provides a better means of understanding, an enterprise’s contribution to society. A detailed format of Value Added Statement is shown in Table for computation of ‘Creation of Value Added’ and ‘Distribution of Value Added’.
Table-1.2 **General Format of Value added Statement**

**ABC LTD.**

Value Added Statement for the year ended 31\textsuperscript{st} march………

**CREATION OF VALUE ADDED:-**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. Sales (including Excise duty and Sales tax):</strong>-</td>
<td></td>
<td>***</td>
</tr>
<tr>
<td>Less:-</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Rebate</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Returns</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Commission</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Discount</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Goods used for self consumption</td>
<td>***</td>
<td>****</td>
</tr>
<tr>
<td><strong>B. Income from services :-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Royalty</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Dividends and Interest</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Rent Received</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Other Miscellaneous income</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td><strong>Less:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scrap Realized</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Increase in Stock of Finished Goods &amp;WAP</td>
<td>***</td>
<td>****</td>
</tr>
<tr>
<td><strong>C. Cost of Bought – in Materials and Services:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add:- Cost of Bought – in Materials</td>
<td></td>
<td>***</td>
</tr>
<tr>
<td>Description</td>
<td>Value</td>
<td></td>
</tr>
<tr>
<td>--------------------------------------------------</td>
<td>-------</td>
<td></td>
</tr>
<tr>
<td>Opening of Bought – in Materials</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Add: Purchases</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Less:</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Closing Stock</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Raw Material Consumed</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td><strong>Other Materials:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consumables</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Packing</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Stationary</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Fuel and Oil</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Electricity</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Repairs to Plant &amp; Building</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td><strong>D. Cost of Services:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Audit Fees</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Rent, Rates, etc.</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Traveling Expenses</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Advertisement</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Postage &amp; Telegram</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Printing</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Subscriptions</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>-------------------</td>
<td>-----</td>
<td></td>
</tr>
<tr>
<td>Carriage outwards</td>
<td>***</td>
<td></td>
</tr>
<tr>
<td>Other Expenses</td>
<td>***</td>
<td>****</td>
</tr>
<tr>
<td>Added Value Created (A+B+C+D)</td>
<td>****</td>
<td></td>
</tr>
</tbody>
</table>

(Sources: “Advanced Management Accounting” by Ravi M. Kishore, p.1163.)
## DISTRIBUTION OF ADDED VALUE:-

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. To Employees:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Wages and Salaries</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ MD’ s Remuneration</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Directors Sitting Fees etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Contribution to P.F. ESI and other benefits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Staff Welfare etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>B. To Government:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Customs Duty</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Excise Duty</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Sales Tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Income Tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Wealth Tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Rates and Taxes etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidizing on Export etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>C. To Providers of Capital:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Interest on Bank Borrowings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Interest on Term Loans</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Interest on Debentures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Interest on Others</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Dividends</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>D. Retained in Business:-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Depreciation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Retained Profit</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Disposal of Total Added Value\((A+B+C+D)\)

(Sources: “Adanced Management Accounting” by Ravi M. Kishore, p.1163.)
2. **Report Format of Value Added Statement**

In this method the Value Added statement is divided into two parts. The first part showing generation of Value Added and the second parts shows the application of Value Added. Value Added commonly prepared in following format. **Table-1.3**

**PQR LTD.**

Value Added Statement for the year ended 31st march………

(Source: Analysis and Interpretation of Value Added statements pg.14-17)

<table>
<thead>
<tr>
<th>Items</th>
<th>Rs.</th>
<th>Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1. Generation of Value Added</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales Revenue</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Add:</strong> Income from services</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less:</strong> Cost of bought in goods and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Services from outsiders</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>GVA</td>
<td></td>
</tr>
<tr>
<td><strong>Less:</strong> Depreciation</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>NVA</td>
<td></td>
</tr>
<tr>
<td><strong>2. Application of Value Added</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payment to Employees</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payment to Government</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payment to providers of capital:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Lenders</td>
<td></td>
<td></td>
</tr>
<tr>
<td>➢ Shareholders</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Retained Earnings (including depreciation)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Net Value Added
3. **Account Format of Value Added Statement**

Table-1.4

**ABC LTD.**

**Value Added Statement for the year ended 31st march**

<table>
<thead>
<tr>
<th>Generation of VA</th>
<th>Rs.</th>
<th>Application of VA</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td></td>
<td>Payment to Employees</td>
<td></td>
</tr>
<tr>
<td>Add: Income from Services</td>
<td></td>
<td>Payment to Government</td>
<td></td>
</tr>
<tr>
<td>Less: Cost of bought in Goods &amp; services From outside</td>
<td></td>
<td>Payment to providers of capital:</td>
<td></td>
</tr>
<tr>
<td>GVA</td>
<td></td>
<td>1. Lenders</td>
<td></td>
</tr>
<tr>
<td>Less: Depreciation</td>
<td></td>
<td>2. Shareholders</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Retained Earning</td>
<td></td>
</tr>
</tbody>
</table>

*Net Value Added* | *Net Value Added* | (Source: Analysis and Interpretation of Value Added statements pg.14-17)

1.14 **ADVANTAGES OF VALUE ADDED STATEMENT:**

Value Added Statement is the barometer of corporate performance for Share – holder and stake – holders. That is why it shows in many corporate annual reports, as a part of additional financial information. The VAS has number of advantages out of them some are given below.

1. **Tool of Measurement For Business Performance:**

Value Added data are being used for measuring the performance both a business firm and non – business firm. It can be said that value added statement is the only reliable indicator of performance because it shows wealth created by the enterprise. For the measuring efficiency, a number of rations based on value added can be constructed. From the systematic analysis of these ratios, it can be possible to draw some valuable conclusions.
2. **Measurement of Productivity:**

   Capital and labour are the most important factors of production and profitability of the business. The productivity of capital can be obtained by the ratio of Value Added to Capital Employed. There is a positive relationship between this two. So, the higher the ratio the greater is the Productivity of capital. And the productivity of labor can be measured by the ratio of labor cost to Value – Added. Here, there is a negative relationship. As the ratio decrease the productivity increases and Vice-Versa.

3. **Objectivity:**

   If value added data is used properly, it will give useful insights into the wealth generation process of an enterprise. An important aspect of the value added data is objectivity. This is only due to the objectivity the decision makers can take decision more accurately.

4. **Useful to Management:**

   Value added can be used by management in different ways. As performance evaluation is the key to performance improvement, the management has to evaluate his own performance. Value added statement can be very useful to management in evaluating the results of past decisions and actions. Systematic and evaluation can be done and it helps to identity trouble spots and over come them. Management may prepare separate value added statement in relation to the different segments of business.

5. **Useful to Share Holders:**

   Share Holders who are the owners of enterprise provide Equity Share Capital to the business unit. VAS is very useful to them in making the decision of purchasing right issues. If the retained earnings or ploughed back to profit increases, the financial strength of the company will definitely improve.

6. **Useful to External Parties:**

   The External Parties include Investors, Creditors, Customers, Professional, Financial Analysts, Security Market Participants and Taxing Authorities. The financial statement of business unit published mainly for these External Users because they were benefited by the information contained in the published financial statements.
7. **Useful to Government:**

With the help of VAS Government can frame it various policies like Wage Policy, Labour Incentives, Labour Laws, Policy on Tax Structure, etc. Government Socio Economic Policy is also framed. This Value Added Statement represents business firm’s share to Nation Income. Value Added provided a link between financial statement and the economists.

Value Added Statement reflects a broader view of the companies objectives and responsibilities, so it improve the attitude of the employees towards the employing company.

Value Added Statement makes it easier for the company to introduce the productivity linked bonus scheme for employees based on Value Added for this Value Added payroll ratio is used as a basis.

Value Added provides a very good measure of the size and importance of a company.

Value Added Statement link a companies financial accounts to the National Income. A companies Value Added Statement indicates the companies contribution to National Income. As Value Added Statement is based on the System Of National Accounts given by UNO to calculate GDP and India signatory to it.

1.15 **DISADVANTAGES OF VALUE ADDED STATEMENT:**

Value added statement suffers from a number of disadvantages and because of this many accountant are not ready to put much reliance on such income as an index of business performance. Some of the main limitations of value added statements are as under.

1. VAS is included in annual report and that would involve extra work. Therefore extra cost and delay and also there is possibility of losing confidentiality in view of the additional disclosure involved.

2. The data contained in the VAS are not capable of adding anything important to the information content of the basic financial statements which are made
Conceptual Framework Of Value Added Reporting - B

Chapter-1

up of balance sheet, income statement or profit & loss account and the fund flow and cash flow statement.

3. No doubt, profit is a part of value added but the maximization of value added does not lead to maximization of profit. A business unit can able to maximize value added by taking a number of inefficient policies but it can not maximize profits in such a way.

4. VAS generally, emphasizes on value creation and value allocation.

5. VAS inclusion in annual report can cause confusion with earnings statement.

6. Value added accounting does not recognize the special role that profit plays in the field of business. Profit is treated more important then items in VAS.

7. There is lack of uniformity among business firms while preparing and presenting of VAS. This limitation is considered as the most serious out of above.

1.16 DIFFICULTIES IN PREPARATION OF VAS:-

The following difficulties or problems generally arise in preparation of Value Added Statement.

1. Treatment of investment Income:

In the case when a company has income from associated companies or royalties, there is a question will arise that the income should be added to turnover in the source section of the Value Added Statement or not? The alternatives are to added it to turnover or to obtain a Value Added calculation from sales less purchases and then to add the other income. If the non sales items are very few, the distinction may not matter too much, but the company should be consistent in its presentation.

2. Treatment of Work – in – progress and Stocks:-

In company’s annual accounts, Work – in – progress. However of profit only in the case of long term Work – in – progress. However, if true Value added is the increase in value created by the company, changes in stocks and Work – in – progress should be included at market value. However, for published accounts, generally accepted accounting principles (Gap) argues the inclusion of “Unrealized profit”. As long as that distinction is understood, user of value added statement can draw their own conclusion.
3. Treatment of payroll costs:

The other main difficulty with published statements concerns is the treatment of payroll costs which are related to the sales achieved? Is the main question. Where companies reveal separately the total amount of payments to employees in published accounts it seems illogical to include a different amount in the value added statement. At the same time, if there is a change in finished stocks and work-in-progress, part of the periods actual costs will be include in the valuation. Most of the companies show the total payroll costs for the period.

4. Depreciation:

The preparation of Value Added Statements in the business world created some remarkable misunderstanding about the nature and purpose of the Value Added Concept. It clearly shows that a standard accounting practice needs to be specified in order to prepare the Value Added Statements because it is an important indicator of corporate performance. The treatment of Depreciation in both the cases of Gross Value Added (GVA) and Net Value Added (NVA). Table sets out the relevant considerations.

Table-1.5

<table>
<thead>
<tr>
<th>Gross Value Added (excluding depreciation sums total of bought – in items)</th>
<th>Net Value Added (including depreciation sums within the total of bought–in items)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Depreciation sums derive from methods of calculation influenced by opinion. The group of bought–in items is based on verifiable facts of expenditure. Value Added should reflect the consequences of goods and services bought–in and consumed during the period.</td>
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</tr>
<tr>
<td>2. To exclude depreciation from the total of bought–in items would result in double counting. This would result in double counting. This would arise when the seller of a fixed asset shoed its value in his value added calculation of value added by separate firms would not display the total creation of wealth.</td>
<td>By including depreciation sums in the bought-in section of corporate Value Added Statement, we do achieve the principle objective of identifying and locating the sources of wealth creation.</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>3. Excluding depreciation from the bought-in items and joining it with retained profits in the appropriate of value added emphasizes the CASH FLOW concept. This is a valuable appraisal tool for use as a measure of corporate efficiency.</td>
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<td>4. When depreciation is excluded from bought-in items, the sum of value added thus determined would imply a distribution of capital assets, for consumption by all business firm’s team members. The ultimate wearing out or obsolescence of the fixed assists would occur with no provisions for its replacements.</td>
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</tr>
</tbody>
</table>
1.17 MEANING & DEFINITION OF VALUE ADDED RATIOS

A financial ratio (or accounting ratio) is a relative magnitude of two selected numerical values taken from an enterprise's financial statements. Often used in accounting, there are many standard ratios used to try to evaluate the overall financial condition of a corporation or other organization. Financial ratios may be used by managers within a firm, by current and potential shareholders (owners) of a firm, and by a firm's creditors. Security analysts use financial ratios to compare the strengths and weaknesses in various companies. If shares in a company are traded in a financial market, the market price of the shares is used in certain financial ratios.

According to ANTHONY, “A ratio is simply one number expressed in terms of another. It is found by dividing one number, the base, into the other. A percentage is a one kind of ratio, in which base is taken as equaling 100 and the quotient is expressed as per hundred of the base.”

“Ratio are simply a means of highlight in the arithmetical terms relationship between figures drawn from financial statements.”

In word of J.BETTY the term ‘accounting ratios’ is used: “ to describe significant relationship which between figures shown on a balance sheet, in a profit and loss account, in a budgetary control system or in any other part of the accounting organization.”

1.18 OBJECTIVE OF RATIO ANALYSIS

The following are some of the important objectives of Ratio Analysis:

1. Expressing Trends:

Financial ratios are usually to show from the past financial records of the cost, sales, profit and other important factors so that quick forecasting can be made for future.

2. Showing changes:
Financial ratios are useful in highlighting various changes in financial activities during different time periods.

3. **Setting Standards:**

The actual results are compared with the standard and preventive steps are taken by the management.

4. **Effective control**

Ratio analysis is used to have an effective control over performance and costs.

5. **Measuring Efficiency**

Ratio analysis is used as a tool for measuring the efficiency of the management.

6. **Knowledge of liquidity**

By evaluating liquidity the management can judge the operational efficiency of the concern.

1.19 **LIMITATION OF RATIO ANALYSIS:**

The following are some limitation of Ratio Analysis:

1. Limited use of a single Ratio.
2. It provides only a Media of Interpretation.
3. Affected by Window Dressing.
4. Lack of Qualitative Analysis of the problem.
5. Effect of Inherent Limitation of Accounting.
6. Lack of Proper Standards
8. Effect of Personal Ability and Bias of the Analyst.

1.20 **RATIOS BASED ON VALUE ADDED:**

Value Added information can be used to compute various ratios and they are to gauge the social contribution and corporate social, economic and general prosperity. The ratios are as under.
1. **Value Added Per Rupee of Capital Employed:**

   This ratio indicates the amount of Value-Added Generated per rupee of capital employed. Greater the ratio higher will be social contribution. Following formula is being used to find out ratio. It also called Capital Productivity.

   \[
   \text{Capital Productivity} = \left( \frac{\text{Value Added}}{\text{Capital Employed}} \right) \times 100
   \]

   1. Value Added is (NVA) Net Value Added.
   2. Capital Employed is the difference between Total Assts and Total Liabilities.

2. **Operating profit to Capital Employed Ratio:**

   Operating profit to capital Employed ratio other operating profit margin on return on capital employed. It is a basic measure of profitability this ratio higher it is better. This relationship can be calculated by following formula.

   \[
   \text{Operating profit to Capital Employed Ratio} = \left( \frac{\text{Operating profit}}{\text{Capital Employed}} \right) \times 100
   \]

   Here,

   ➢ Capital Employed is the difference between Total Assts and Total Liabilities.

3. **The Net Value Added Per Rupee of Sale.**

   This ratio shows the contribution of firm’s sales income toward Value Addition. An effective sales management strategy would enable a company to enhance this percentage. It also called Gross Margin. This ratio can he finding with the help of below given formula.

   \[
   \text{Gross Margin} = \left( \frac{\text{Value Added}}{\text{Total Sales}} \right) \times 100
   \]

   Here,

   ➢ Value Added is considered as Net Value Added (NVA)
→ The value of Sales including Excise Duty is taken here.

4. **Net Value Added to Cost of Goods Sold:**

This ratio shows the relationship between Net Value Added and cost of goods sold. This can be calculated as following:

\[
\text{Net Value Added to Cost of Goods Sold} = \left(\frac{\text{Net Value Added}}{\text{Cost of Goods Sold}}\right) \times 100
\]

Here,

\[\text{Cost of Goods Sold} = \text{Raw materials Consumed} + \text{cost of power and fuel} + \text{cost of stores and sparts} + \text{wage} + \text{salaries} + \text{excise duty} + \text{purchase of finished goods and other factory expenses}.\]

5. **Depreciation to Gross Value Added ratio:**

This ratio shows the relationship between the Depreciation and gross value added. This formula as given below.

\[
\text{Depreciation to Gross Value Added ratio} = \left(\frac{\text{Depreciation}}{\text{Gross Value Added}}\right) \times 100
\]

6. **Gross profit to Net Value Added Ratio**

This ratio shows the relationship between the Gross profit and Net Value Added. The formula is given below.

\[
\text{Gross profit to Net Value Added Ratio} = \left(\frac{\text{Gross profit}}{\text{Net Value Added}}\right) \times 100
\]

7. **Net Profit Before Taxes to Net Value Added Ratio:**

This ratio shows relationship between the Net Profit Before Taxes and net value added. The formula is given below.

\[
\text{Net Profit Before Taxes to Net Value Added Ratio}
\]
Here,

\[ \text{NPBT} = \text{Net Profit Before Taxes.} \]

8. **Net profit to Net Value Added Ratio:**

This ratio shows how much percentage of value added remained for providers of own capital after meeting all the obligations and depreciation. This relationship has been computed by dividing net profit after interest and taxes by Net value added. It can be calculated with the help of following formula.

\[
\text{Net profit to Net Value Added Ratio} = \frac{\text{NPAIT}}{\text{Net Value Added}} \times 100
\]

Here,

\[ \text{NPAIT} = \text{Net Profit After Interest \& Taxes}. \]

9. **Net Value Added per Employee :-**

This ratio indicates productivity and effectiveness of the employee. This ratio also called Productivity. It can be obtained with the help of this ratio. The greater the ratio the higher will be the labour productivity of the employee. Labour productivity can be calculated with the help of following formula.

\[
\text{Labour productivity} = \frac{\text{Net Value Added}}{\text{Total No. of Employees}} \times 100
\]

Here,

1. Value Added is taken as the Net Value Added (NVA).
2. At the end of the financial year the strength of the firm shows No. of Employees.

10. **Employees Benefit to Net Value Added Ratio:**

This ratio indicates how much percentage of net value added remained for employees after paying value for other group of society.
It useful measuring efficiency and utility of labour power of an enterprise. This ratio calculated as follows:

**Employees Benefit to Net Value Added Ratio**

\[
\frac{\text{Employees Benefit}}{\text{Net Value Added}} \times 100
\]

Here,

\begin{align*}
\text{Employees Benefit} & = \text{Wages and salary} + \text{MD’s remmuneration} + \text{Director fees} + \text{contribution to PF and ESI} + \text{Staff Welfare}.
\end{align*}

11. **Rate of Investment per Employee:-**

This ratio is useful to find out the Rate of Investment per Employee. This can be finding out by Capital Expenditure and No. of Employee. The greater the ratio the higher will be the rate of investment per employee. The formula is given below.

**Rate of Investment per Employee**

\[
\frac{\text{Capital Expenditure}}{\text{Total No. of Employees}} \times 100
\]

Here,

1. Capital Expenditure of current financial Year is taken.
2. No. of Employees at the end of year is taken here.

12. **Value Added Per Rupee of Fixed Assets:-**

The ratio of fixed Assets will be obtained with the help of Value Added and Fixed Assets of the firm. This ratio shows the relationship between Net Value Added to fixed Assets. If the Net Value Added is more than Fixed Assets, it is considered good. This relationship can be calculated by following formula.

**Value Added Per Rupee of Fixed Assets**

\[
\frac{\text{Value Added}}{\text{Fixed Assets}} \times 100
\]

Here,
1. Value Added is taken as Net Value Added (NVA)

2. Fixed Assets includes Buildings, Plant & Machinery, and Water supply & Drainage system, Furniture & Fixtures, Vehicles, Railway Sidings and Computer Software. All Fixed Assets are taken after the dedication of Depreciation.

13. **Gross Value Added to Total Revenue Ratio:**

The proportion of gross Value Added to Total Revenue shows the relationship between above shown two items which reflects that how much percentage of Total Revenues consist of value generated by the concern meaning there by the remaining percentage that is: Total revenue – Gross Value Added, is contributed by the out side parties. It is must to say that a higher proportion of Gross Value Added in Total Revenue will be considered good and will show better social performance. It will also show the utility added by the concern in the total efforts of the organization and related parties. It may be calculated with the help of following formula.

**Gross Value Added to Total Revenue Ratio**

\[
\frac{\text{Gross Value Added}}{\text{Total Revenue}} \times 100
\]

Here,

1. Gross Value Added (GVA) is taken.
2. Total Revenue includes Sales (including Excise Duty) and other income of the company.

14. **Net Value Added to Total Revenue Ratio:**

This ratio shows the relationship between net Value Added and Total Revenue. It may be said that a higher proportion of Net Value Added in Total Revenue will be considered good and will show better social performance. It can be calculated by dividing the Net Value Added by the amount of Total Revenue. It may be expressed in the shape of formula as follows.

**Net Value Added to Total Revenue Ratio**
Here,

I. Net Value Added (NVA) is taken
II. Total Revenue includes Sales (including Excise Duty) and other income of the company.

15. Government Share to Net Value Added Ratio :-

Every corporate unit pays some value to government in form of taxes. This ratio shred how much percentage of government share to net value added. This ratio calculated as follow:

**Government Share to Net Value Added Ratio**

\[
\frac{\text{Taxes Paid to Government}}{\text{Net Value Added}} \times 100
\]

Here,


16. **Payment to Shareholders to Net Value Added Ratio:**

   Every corporate unit has to pay dividend to its shareholders or providers of capital. This ratio shows the earning management policy of the concern. This relationship creates following formula.

**Payment to shareholders to Net Value Added Ratio**

\[
\frac{\text{Dividened}}{\text{Net Value Added}} \times 100
\]

17. **Retained Earning to Net Value Added Ratio:**

   This ratio shows the relationship between Retained Earning and Net Value Added. It is calculated as follows formula:

**Retained Earning to Net Value Added Ratio**
18. **Interest to Net Value Added Ratio:**

This ratio find out that how much percentage of Net Value Added is cost of capital. This ratio represents efficiency or inefficiency of capital management. This ratio is calculated as follows formula:

\[
\text{Interest to Net Value Added Ratio} = \frac{\text{Interest}}{\text{Net Value Added}} \times 100
\]
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