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GENERATING VALUES TO AN ORGANIZATION THROUGH VALUE ADDED STATEMENTS – A CASE STUDY APPROACH WITH SPECIAL REFERENCE TO INFOSYS LTD

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ABSTRACT

The primary objective of any business is to earn profit and create maximum wealth for its shareholders. But of late, organizations have started showing considerable interest on the other stakeholders of the organization like employees, government, and society. For this purpose, the organizations have to move from the profit and loss account statement to a new concept of contributing to the various stakeholders of the society. This increasing interest on the society has made the organizations redesign its objectives as well as the financial reporting practices. The most important factor of contribution by the organization to the society is by increasing the economic status of the society. Therefore, to measure and report the societal objectives of the organization, a new age financial reporting standards called ***"value added"*** *has emerged to measure the contribution of the organization towards the economic development of the society. Value added statement is an important measure of corporate performance towards the society rather than the traditional financial reporting style. Value Added statement is prepared as an improvised version of P & L a/c. The concept of value added is considerably old, but the adoption of same to financial reporting is still in infant stage. This case study does an empirical study of Infosys pvt ltd on is application of value added reporting.*

Keywords

Infosys, financial reporting, profit & loss A/c, Value added statements

INTRODUCTION

Value added statement of reporting in an important measure to judge a business performance and contribution towards the society. The value added statement moves away form the traditional way of understanding the profit generated by a business to the wealth created by business. All business entities have been preparing financial statements to derive their profit position, but the growing importance to societal objectives has led to the realization on contribution to the society by business entities. The value added statement in broad tries to understand the different investment made by different stakeholders like shareholders, debenture holders, creditors and other financial institutions. It can particularly be useful in understanding employee oriented approach, which will allow more objective assessment of business in terms of productivity and profitability. Therefore, value added statement has a direct relationship with the concept of understanding the contribution of business towards the society.

PURPOSE OF THE CASE STUDY

The fresh development in the financial reporting approach called "Value Added Statement" is an area not aware by many. Hence, a focused study is attempted here to provide a simpler and holistic view:

- To understand the purpose of Value Added Statements
- To study the different types of Value Added Statements
- To understand the method of Preparing the Value Added Statement
- To do a comparative study of the Traditional technique of financial reporting and Value Added approach
- To assess the of the value added statements
- To examine a practical case of the implementation of Value Added Statement by Infosys

RESEARCH METHODOLOGY

The study is based on the available secondary source of information. The data has been collected from the annual report of Infosys for the year 2010-2015. For collecting relevant data for the purpose of conducting this study internet surfing has also been made for obtaining the requisite and latest information. Editing, classification and tabulation of the financial data collected has been done as per the requirement of the study.

CONCEPTUAL FRAMEWORK OF VALUE ADDED REPORTING

a. **Concept of Value addition:** 'Value Added' is the 'wealth created'. Ahmed Riahi Belkaoui (2010) opines that the accurate measurement of wealth created and distributed to stakeholders is only through 'Value Added' concept. The simplest and most immediate way of putting profit into proper perspective vis-à-vis the whole enterprise as a collective effort by capital, management and employees is by 'Value Added Statement'. A reporting entity creates wealth through the collective effort of capital, management and employees. Such accumulation of wealth adds value to the entity as a whole. The value addition achieved by the entity determines its position in the industry in the long run. The recent developments in Financial Reporting emphasize on the area "Value Addition". One of the significant aspects of value additions is the "Value Added Statement". 'Value Added Statement' is the statement showing the turnover, costs, profits earned and distributed to stakeholders but in a manner different from the traditional way of communicating it. It is an optimistic way of showing the financial results of an entity. In other words, it is a modified version of the Profit & Loss a/c. The beauty of this area of 'Value Addition' is that it is not covered by any statute or accounting standard. It is not mandatory to prepare them as such. It is the tool to change the financial communication in an optimistic way in view of global scenario of reporting development. According to Gray and Maunders (1980) the statement of Value Added provides a useful measure to help in growing performance and activity. The figure of 'Value Added' can be a pointer to the net output of the firm.

b. **Concept of Value added Reporting:** The concept of value added has a direct link with the concept of social responsibility. Value Added Analysis is the analysis of wealth creation and application of wealth by any enterprise. It is considered as a part of social responsibility reporting. The value added reporting is a rearrangement of financial information provided in the traditional reporting by mentioning the contribution of the business to the society. It has been recognized that the activities of an enterprise have both economic and social impacts on the users of financial statements. An enterprise is accountable to the society as it uses common assets of the community at large such as railways, harbour roads and other facilities. Every business while performing in a society should create wealth for that society.

c. **Objectives of value added reporting:**

1. **Generation & Distribution of wealth:** Value Added Statement is primarily prepared to show how profits are generated (wealth) and the manner in which they are distributed to the stakeholders like shareholders, employees, management etc.,
2. **Optimistic view on expenditure:** The items of expenditure which are normally seen as 'expenditure' are treated as "share of wealth distributed" to stakeholders. Example: Tax paid to the government is sharing of wealth generated with the government.
3. **Contribution to society:** The distribution of wealth is done in such a way that the societal elements helping to run the business are awarded with considerable share in wealth (profits)

d. **Value added Statement**: The formal recognition of the Value Added Statement(VAS) was first made in a discussion document entitled "The Corporate Report" which was published by the Accounting Standards Steering Committee of the UK in 1975 (Basu, 1992). According to the Corporate Report, the value added statement is to be prepared on the assumption that the business is a partnership which is made up of the employees, providers of capital, government and the enterprise itself. The statement is designed to disclose how much wealth (i.e. value) the enterprise has generated as a result of the joint efforts of its partners (ASSC, 1975). David Pendril defines it as "The statement which shows the income of the company as an entity and how that is divided between the people who have contributed to its creation" (Pendril, 1977). In India, value added statement is a voluntary corporate supplementary statement, which provides the information in such a manner that would easily be understood by a layman and that shows a broad measure of performance of a corporate entity. The ASC report is concerned with the specification of income attributable to employees, government, and the providers of capital. It is thus, an extension of the income Statement, regarding the earnings of profits in business as a cooperative effort (Rao, 2001). The following are the definition of VAS has been defined by different authors: Value Added Statement may be defined as a statement which shows the size of the ‘value added cake’ and how the ‘cake’ has been divided amongst the various stakeholders (Sizer, 1979). Value Added Statement may be defined as the performance of an organization to what extent the enterprise has added value during a particular period to the providers of capital, employees, government and reinvestment of the growth and expansion (Agarwal, 1993). Value Added Statement is a report which shows the amount and the sources of value added during some specified period of time. In other words, it is also described as extra wealth created by selling goods and services to the customers. So it is entitled as ‘wealth generated and distributed’ (Rao, 1999).

e. **Advantages of value added statements:**

- Value Added Statement reflects the corporate significance of a company. It depicts the positive perspective of the entity towards the society.
- It improves the attitude of the employees towards the employing companies as it enables a broader view of the objectives and responsibilities on wealth distribution.
- Value Added Statements enable the entity to issue productivity linked bonus schemes for employees based on Value Added Statements. The employees may be given productivity bonus on the basis of Value Added/ Payout ratio.
- It facilitates in the preparation of Value Added based ratios like: Taxation/ Value Added, Value Added/Sales etc., which can be used as diagnostic and predictive tools. Ratio analysis and comparisons are possible through Valued Added Statements.
- Value Added Statement links a company’s financial accounts to national income. A company’s value added indicates the company’s contribution to national income.

f. **Limitations of Value added statements:**

- Value Added Statement cannot be a substitute to the traditional Profit & Loss a/c as it does not show a complete picture as in Profit & Loss a/c
- Identification of each expenditure and classifying it in order to fit in the components of Value Added Statement is a difficult task.
- Value Added Statement does not cover all the components that are suitable for each and every item of expenditure to fit in. Example: Extraordinary items.

TYPES OF VALUE ADDED STATEMENTS

There are two types of Value Added Statements namely, "Gross Value Added Statement", "Net Value Added Statement". Net Value Added Statement is prepared in the same manner as Gross Value Added Statement except that:

- Depreciation is included in 'Cost of bought in material & services' instead of 'Maintenance & Expansion'.
- Excise Duty paid is included in 'Government' instead of 'Cost of bought in material & services' in Net Value Added Statement.

COMPARATIVE STUDY OF THE TRADITIONAL APPROACH AND VALUE ADDED APPROACH

Every entity earns revenue for a specific period of time. This revenue/sales is the prime item that is considered first. The expenses incurred are subtracted from the amount of sales and profit is arrived. This is the 'Traditional approach'. When the expenses related to the cost of goods sold are subtracted from the revenue/sales and the resultant "wealth available for sharing" is shared by the components which facilitated the wealth creation, it is the 'Value Added approach'.

A comparative study of the Traditional approach and Value Added approach is made in order to find the added advantage of Value Added approach over Traditional approach. The following table shows the comparative study made:

Table 1: Comparative Study of the Traditional Approach and Value Added Approach

Element	Traditional approach	Value Added approach
1) Way of approach	In traditional profit & loss, the final profit or loss is arrived at after subtracting all the expenses from sales.	In Value Added, only cost of bought in material and services are deducted from sales to arrive at "Value Added".
2)Components	Traditional approach does not have any specific components under which expenses are clubbed.	Value Added approach has 5 components (employees, management, Government, Providers of Capital and Maintenance & Expansion) under which the related expensed are clubbed.
3) Measurement	It measures the welfare of the shareholder alone.	It measures the welfare of the society as a whole.

4)View	The expenses are viewed as mere expenses that decrease the profits.	Expenses are viewed as costs incurred to procure material, services and wealth distributed for the efforts of elements contributing to profit making.
5)Proportion	Traditional approach does not reveal the proportion of each major expense in profit.	Value Added approach conveys the proportion of application of wealth in each component that contributed to value addition of wealth.

PORFORMA DEPICTING THE ELEMENTS OF THE TRADITIONAL APPROACH AND VALUE ADDED APPROACH

The following table gives a clear picture of the difference between the portrayal of expenses from the revenue earned and the arrival of profits under Traditional approach and Value Added approach

Table 2: Proforma depicting the elements of the Traditional Approach and Value Added Approach

Traditional approach	**Value Added approach**
Sales (+) Other income (-) Cost of goods sold (-) Salaries (-) Interest (-) Managerial Remuneration (-) Depreciation (-) Other expenses (-) Tax (-) General reserve appropriation (-) Dividends (-) DDT Retained profits	**Sales** (-) Cost of goods sold (+) Other income Wealth available for sharing **Shared by:** Employees (Salaries) Management (Managerial remuneration) Government (Tax) Providers of capital (Interest, Dividend) Maintenance & Expansion (Depreciation, Appropriations)

PROFORMA OF VALUE ADDED STATEMENTS

Table 3: Proforma of Value Added Statements

Particulars	**Amount (Rs.)**	
Sales	xxxx	
(-) Cost of bought in material and services	(xxx)	
Value Added from manufacturing and trading activities	xxxx	
(+) Other income	xxx	
GROSS VALUE ADDED	xxxx	
Shared by:		
Employees	xxx	%
Management	xxx	%
Government	xxx	%
Providers of Capital	xxx	%
Maintenance & Expansion	xxx	%

PARTICULARS UNDER EACH ELEMENT OF THE VALUE ADDED STATEMENTS

- **Cost of bought-in material & services:**

All the direct expenses related to manufacture/production form part of this item. Consumption of raw material, power & lighting, selling expenses etc., are the examples of cost of bought- in material. Expenses like Audit fee, rent paid are the cost of bought in services.

- **Other Income:**

The incomes which do not form part of sales like dividends and profits received from investments made, miscellaneous income etc., are included in 'Other income'.

- **Employees:**

Salaries & wages paid to the employees, staff welfare expenses and any other specific expenses related to employees are shown here as wealth shared with employees.

- **Management:**

Managerial Remuneration, Sitting fee of Directors etc., is the part of wealth distributed to management.

- **Government:**

Income Tax, other kinds of taxes paid to the Government , any legal fee paid as a part of any procedure etc., form part of the wealth shared with the government.

- **Providers of Capital:**

The dividends paid to the shareholders, interest paid to the loan lenders and debenture holders are the part of wealth shared with the providers of capital.

- **Maintenance & Expansion:**

Depreciation, Provisions made, amount taken to the General Reserve, Profits retained are part of Maintenance & Expansion.

VALUE ADDED STATEMENT OF INFOSYS

Table 4: Value-added statement of Infosys

in ₹ crore

	2011	*%*	*2010*	*%*	*Growth %*
Value-added					
Income	27,501		22,742		20.9
***Less* Operating expenses excluding personnel costs**					
Software development and business process management expenses	2,083		1,461		
Selling and marketing expenses	294		249		
General and administration expenses	1,304		1,087		
	3,681		**2,797**		
Value-added from operations	23,820		19,945		19.4
Other income (including exceptional items)	1,211		990		
Total value-added	**25,031**		**20,935**		**19.6**
Distribution of value-added					
Human resources					
Salaries and bonus	14,856	59.4	12,093	57.8	22.8
Providers of capital					
Dividend(1)	3,445	13.8	1,434	6.8	140.2
Minority interest	–	–	–	–	–
Interest on debt	–	–	–	–	–
	3,445	**13.8**	**1,434**	**6.8**	**140.2**
Taxes					
Corporate income taxes	2,490	9.9	1,681	8.0	48.1

Dividend tax(1)	568	2.3	240	1.2	136.7
	3,058	**12.2**	**1,921**	**9.2**	**59.2**
Income retained in business					
Depreciation and amortization	862	3.4	942	4.5	(8.5)
Retained in business	2,810	11.2	4,545	21.7	(38.2)
	3,672	14.6	5,487	26.2	(33.1)
Total	**25,031**	**100.0**	**20,935**	**100.0**	**19.6**

Source:Infosys

OBSERVATIONS FROM THE INFOSYS CASE

- The Value Added statement of Infosys included the previous year's figures to simplify the measurement of relative performance of Infosys.
- It clearly indicates the growth percentage of figures in every component of Value Added statement.
- The 'Employees' & 'Management' components have been included under a single item called "Human Resources".
- The wealth shared with the "Human Resources" forms the lion's share of total wealth created.
- Nearly 60% of the Value Added is distributed to the "Human Resources" as salaries and bonus.
- The other components namely – Providers of capital, Taxes & Income retained in business form only a little part of the value added to the entity.
- 'Maintenance & Expansion' component is shown as 'Income retained in business.
- Value Added Statement portrayed above helps to boost the confidence of the workforce of an organization as their share in wealth is highest.
- The degree of satisfaction of the stakeholders improves to a great extent through Value Added Statements.
- Thus, Value Added Statements enable to improve the workforce stability, stakeholder's reliance & the overall growth of the organization on equal basis.

From the practical case of the Value Added Statements of Infosys, we can infer that the adoption of the concept of Value Added is being improved in the recent times in India. The Multi National Companies are now considering the importance of portraying the value added by them to societal forces and stakeholders through the preparation of Value Added

Statements. However, there are still many business entities which do not yet prefer this concept and they follow only the traditional approach of showing the profits earned.

FINDINGS FROM THE CASE ANALYSIS

- Value Added approach has an added advantage of showing the proportion of each component in Value Added to the entity.
- Value Added Statement satisfies the stakeholders and societal factors that support the operations of the entity through the equitable distribution of wealth.
- The Traditional approach has strong foundation and direct application of the accounting concepts which makes it compatible with the other components of financial reports like Balance sheet, cash flow statements. The same may not be achieved by Value Added statements.
- On an overall basis, Value Added Statements are prepared and presented by the entities as an additional financial report but not as a substitute to the Traditional Profit & Loss statement.

SUGGESTIONS FOR IMPROVEMENT

- Value Added should be prepared on both gross and net basis to serve a wide range of uses.
- Depreciation is not recommended to be a part of distribution of value added.
- Inflation adjustments are necessary if value added is to be shown in more realistic manner.
- Non operating items should be disclosed separately below the calculation of value added.
- Easy adoption techniques to be introduced for more Value Added Statements to be generated by the organizations in India.

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