

# **VALUE ADDED STATEMENT**

# INTRODUCTION

The concept of value-added has not yet been widely used in the management of Indian firms. In several European countries and in the U.K. this concept has been in use for quite sometime because they have introduced value-added tax in their fiscal system. In India, too, some well-known companies have started presenting value-added statements in their annual reports e.g. ACC in its latest report has given a value added statement.

# INTRODUCTION

The economists have been using this concept for measuring the Gross National Product. The four productive agencies working on the natural resources, convert them into usable products and add value which is termed as national wealth. This is distributed to these four agents of production. This logic can be applied to individual firm also.

# DEFINITION OF VALUE ADDED

Value Added = Net Sales - Cost of items bought from outside.

We discuss below some of the definitions :

- “Value added may be defined as the ultimate value of sales of goods and services by the firm (represented by its sales turnover) less the cost of all goods and services bought from outside suppliers.”
- Kohler writes, “Value added is that part of the cost of manufacture of semi-manufactured product attributable to work performed on constituent raw materials.”
- “Value added is the excess of firm's sales revenue and income from services over the cost of materials and services bought from outside.”

# DEFINITION OF VALUE ADDED

Here sales revenue includes selling price of goods plus duty and sales tax less goods returned, goods withdrawn for personal use, commission, rebate, discount etc. In the income from services are included such other incomes as rent, interest etc. Cost of services bought include power, fuel, repairs and maintenance, postage and stationery, bank commission, insurance premium, advertisement, printing, audit fees, legal fees etc.

## Purchase

- Materials
- Services
- Other stores



## Firm's Services

- Employees
- Machines
- Owners who provide capital and money
- Government, which provide convenient environment



## Output

- Finished Goods and
- Services



## Who will get as compensation

- Salaries and wages
- Depreciation
- Dividend and interest
- Taxes and duties

# UTILITY OF VALUE ADDED

- The concept of value added is useful in comparing the firm's efficiency with that of other firms of the same industry and also with that of the industry as whole.
- This concept can also be used for developing incentive schemes for workers, especially in relatively labour intensive firms. For this purpose the value added which can be attributed to the performance of labour, is calculated. The sales value at standard selling price is first computed. From this, the cost of actual raw materials and other items used should be deducted at standard rates. The remaining amount is the pool of funds from which bonus may be given to workers.

# UTILITY OF VALUE ADDED

- The concept is useful to the government in many ways. It gives an idea of what the industry can bear in respect of taxes to be levied. The success or otherwise of the government policy of decentralisation and development of specific industries can be judged on the basis of value added.
- The lenders and other creditors of business have also found this concept useful. It will help them in calculating to what extent their share in the increase in value added can be raised.



# UTILITY OF VALUE ADDED

- The owner of business finds the concept useful in that they get an idea of the share of each contributor to it. So that eventually they know the share of value added that remains for them. This will help in making decisions, whether to invest in such business looking to the extent of risk involved in it.
- The value added tax has already been introduced in Britain from 1973. Other countries can likewise do so and make their tax structure more logical and rational.

# UTILITY OF VALUE ADDED:

- In case of companies which have decentralised its working and have introduced evaluation of divisional performance, the concept of value added may provide useful base for setting internal transfer price.

The concept of value added has been found to be useful in measuring efficiency of business. Yet too much should not be expected of it. The limitations of this concept must be kept in mind. Generally profit increases with the increase in the value added. But it may not always be so. This is because profit is only one component of value added and is not the only component. Interest, salaries and wages are also other constituents of value added.

# DIFFERENCE BETWEEN VALUE ADDED AND PROFIT AND LOSS A/C

Both are the annual financial statements of a business enterprise. But there are some points of difference:

- Profit and loss account shows the expenses of incomes of operations of the business and the final result of its operations. It shows the results from the viewpoint of owners only. VAS is prepared from the same figures, but it shows the contribution made by various parties to added value. It is thus wider in scope and gives more details than profit and loss account.

# DIFFERENCE BETWEEN VALUE ADDED AND PROFIT AND LOSS A/C

- The value added statement shows net amount after deducting from net sales value, the materials and other services purchased from outside, while in profit and loss account all expenses, whether direct or indirect and whether relating to external services or to services purchased from outside are deducted from sales. There is no distinction between internal input or external input.
- Value added statement indicates the social objectives of business, while profit and loss account is profit-oriented and is prepared only from the viewpoint of owners.

# DIFFERENCE BETWEEN VALUE ADDED AND PROFIT AND LOSS A/C

- VAS shows the contribution of various parties to the business namely, the employees, providers employees, providers of capital, owners of capital, owners of business, government etc. Profit and Loss account does not show the individual contribution of these parties. It only shows the profit or loss of owners and taxes paid to the government.
- VAS is a new technique and yet a common man can very well understand it. While the profit and loss account is a bit complicated, contains jugglery of double entry book-keeping and a non-accountant reader does not understand it properly.

# **DIFFERENCE BETWEEN VALUE ADDED AND PROFIT AND LOSS A/C**

No business enterprise can survive if it does not add to the value, as it is not able to pay any amount to most of the parties particularly shareholders, government etc. The employees would not cooperate and the business cannot run. While in case of profit and loss account, the business would continue even if there is a loss, because it affects only the owners.

**The following figures for a period were called out from the books of Value Corporation**

	<b>Rs.</b>		<b>Rs.</b>
Sales	24,80,000	Advertisement	25,000
Purch. of Raw Materials	10,00,000	Salaries & Wages	6,30,000
Agent's Commission	20,000	Postage & Telegrams	14,000
Consumable stores	25,000	PF Contribution	60,000
Packing Materials	10,000	Director's sitting fees and travelling exp.	40,000
Stationery	10,000	Subscription paid	2,000
Audit Fees	4,000	Carriage	22,000
Staff Welfare Expenses	1,58,000	Interest on Loan taken	18,000
Insurance	26,000	Dividend to Shareholders	30,000
Rent, Rates and Taxes	16,000	Depreciation Provided	55,000
Managing Director's Remuneration	84,000	Income-tax Provided	1,00,000
Travelling Expenses	21,000	P and L A/C (Retained Earnings)	1,25,000
Fuel & Oil	9,000	Opening stock :	
Electricity	5,000	- Raw Material	85,000
Material used in Repairs :		- Finished Goods	2,00,000
- to Plant - Machinery	24,000	Closing stock :	
- to Building	10,000	Raw Material	1,08,000
		Finished Good	2,40,000

## Solution

### Value Added Statement

Particular	Amount	Amout
<b>Sales:</b>	24,80,000	
Less : Agent Commission	20,000	
	24,60,000	
Add: Inc in Closing Stock (Closing 2,40,000 – Opening 2,00,000)	40,000	
		25,00,000
<b>(A) Less: Purchase of Materials</b>		
Purchase of Raw Material 10,00,000		
- Inc in Stock of Row Material		
(1,08,000 – 85,000) 23,000	9,77,000	
<b>+ Other Materials :</b>		
Consumable Stores	25,000	
Packing Material	10,000	
Stationary	10,000	
Gas, Fuel etc	9,000	
Electricity	5,000	
<b>Material use for Repair:</b>		
Plant and Machinery	24,000	
Building	10,000	
<b>Total Material (A)</b>	10,70,000	
<b>Add: (B) Purchase Services</b>		
Audit Fees	4,000	
Insurance	26,000	
Rent, Rate and taxes	16,000	
Travelling Exp.	21,000	
Advertisement	25,000	



Posting	14,000	
Subscription Paid	2,000	
Carriage	22,000	
<b>Total Services (B)</b>	1,30,000	
<b>Total (A+B)</b>		12,00,000
<b>Total Value Added</b>		13,00,000

### Statement Showing Distribution of Value Added

Particular	Amount	Amount
<b>(A) To the employees:</b>		
Staff Welfare Expense	1,58,000	
Managing Director Expenses	84,000	
Directors Fees and Expenses	40,000	
Salaries and Wages	6,30,000	
PF Contribution	60,000	9,72,000
<b>(B) To Govt : Income Tax Provided</b>		1,00,000
<b>(C) To Provider of Capital :</b>		
Interest on Loan Taken	18,000	
Divided to Share holder	30,000	48,000
<b>(D) To Retain Earning (mqt)</b>		
Depreciation	55,000	
P&L A/C (Retain)	1,25,000	1,80,000
<b>Total Value Added</b>		13,00,000