Technology for Determining the Effectiveness of Representative Offices of the Companies Abroad


Abstract: This article reveals the value of statistical data disclosed in the reporting on the sustainable development of economic entities in unstable economic conditions. The principles and methods of preparing reports on sustainable development of economic entities are determined. The fundamental principle of sustainable development is the requirement of the necessary compliance with the criteria of sustainability. According to the concept of sustainable development for economic subjects, it is necessary to form ways of the long term strategic development in order to increase business value taking into account the requirements of socio-economic and environmental responsibility, which determine the priority of providing information including statistical data for conducting the research. The involvement of economic entities in the concentration of sustainable development through reporting for the stakeholders will allow society to get the greatest effect from the activities of such business entities.

Index Terms: reporting, sustainable development, economic entity, efficiency, statistics, methods, principals, standards.

I. INTRODUCTION

The current state of the world economy is characterized by many challenges from sharpening competition and a new round of trade wars between major economic powers to shifting the emphasis in approaches to the performance evaluation of economic entities from exclusively financial to mostly non-financial, including the environmental and social aspects. The relevant business conditions multiplied by substantial political and economic pressure from a number of countries acutely pose a question to domestic companies about the development of new approaches to determining the effectiveness of their own activities. Conducting such an assessment is necessary in order to provide a timely and adequate assessment of the implemented business model from the perspective of the main stakeholders and to develop an effective strategy for a long-term sustainable functioning in a new business environment. In particular, this issue is relevant to those Russian business entities that implement their activities through foreign representative offices. In addition to the differences in approaches to accounting and public reporting, determining the effectiveness of representative offices of business entities abroad and assessing their strategic performance is complicated by the specifics of the legal status of the representative offices of Russian businesses as well as the legal regulation processes of their activities in different countries. Regardless of the form of ownership, Russian business entities that are legal entities are entitled to independently carry out foreign trade activities abroad in compliance with the current legislation of the Russian Federation. The only exception is the activity that is related to the sale of certain goods to which the state monopoly applies. This activity is subject to obligatory licensing. In turn, the representative office of the organization is its separate subdivision located outside the location of the organization and representing its interests whose activities are fully or partially regulated by the general constituent documents of the organization. It is noteworthy to mention that the legal status of the Russian legal entities abroad is determined, on the one hand, by the legislation of the Russian Federation that should be followed by the legal entities carrying out activities outside the Russian Federation, and on the other hand, by the laws of the country within which these activities are carried out as well as international treaties. The leading role in the legal regulation of the activities of the foreign representative offices of the Russian companies is assigned to the internal legislation of the country in which this activity is carried out. In other words, issues related to the admission of the representation of the Russian business entity to the implementation of the activities in a foreign state and the current procedure for carrying out such activities and its conditions are determined by the legislation of the country in which the corresponding representation is being created, and in accordance with the provisions of the agreements concluded between the Russian Federation and this foreign state. Surely, this state of affairs limits the abilities of the functioning of representative offices of domestic business outside Russia. Since many countries formulate the corresponding section of their legislation, pursuing, among other things, protectionist goals, and in a number of countries, the permission of the relevant national authorities is required for registration of an economic entity with the Russian capital participation [1, 2]. So, the methodology for determining the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad

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should take into account the specifics of local legislation and the possible system of restrictions associated with the implementation of their activities in a foreign country by the Russian representative offices. Despite these restrictions, nowadays there is a fairly wide range of the reasons that encourage business entities of the Russian Federation to open their offices abroad. On the one hand, for a financially successful business with sufficient resources and high market potential, it is logical to expand the geography of its presence at the expense of foreign markets. On the other hand, the creation and development of foreign representative offices may be a possible solution for companies that find themselves on the brink of survival in the Russian market. The other reasons, as well as goals that an economic entity might pursue when deciding to open a representative office abroad, include revenue growth due to the development of new sales market, expansion of its own dealer network, creation of additional distribution channels for products and ensuring the possibility of quality after-sales service in the territories where the products are actually used, increasing the controllability of costs by optimizing the value chain and, consequently, increasing the price policy flexibility, increasing the cost of socio-reputational capital by providing direct access to key customers and suppliers, and etc. Therefore, the question of opening a representative office abroad will always be relevant.

II. MATERIALS AND METHODS

A. General description

The activities of the representative offices of economic entities of the Russian Federation abroad are limited by the basic requirements of the country in which the representative office is located. The need to comply with the legislation of the country in which the representative offices of Russian business entities operate, specific goals and objectives that are faced by them and the specifics of accounting and reporting lead to the occurrence of significant amounts of the unstructured information that significantly complicate the processes of making long-term and medium-term decisions for the management and owners. That is why the creation of an information base for making effective management decisions that is accessible for operational analysis and integrating information, including traditional and strategic management accounting, and forming on its basis a comprehensive and balanced assessment of the effectiveness of the activities of representative offices of Russian business entities abroad is one of the key success factors, the implementation of which creates the conditions for the successful functioning of foreign representative offices of economic entities of the Russian Federation in a complex and dynamic business environment. In this scientific paper, there were used the methods of analysis and synthesis, juxtaposition, grouping, comparison, selective observation, survey, monographic research, and visual presentation of information through drawings and graphs.

B. Algorithm

The article defines the methodology of the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad and focuses on the features functioning in various foreign territories. Determining the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad, first of all, should take into account the method of balancing indicators. Secondly, it is necessary to use an approach to assessing the effectiveness of the activities of representative offices of Russian economic entities abroad based on the analysis of six types of capital. It has an advantage over traditional approaches because it allows us to give a comprehensive assessment of the effectiveness of using both tangible and intangible resources of representative offices. In addition to financial indicators, this approach also discloses a wide range of non-financial aspects of the activity, which actualizes this methodology in accordance with modern requirements for disclosure of information about the performance of activities that are characteristic of countries with developed market economies.

C. Flow Chart

It is necessary to highlight the balanced scorecard (Balanced Scorecard- BSC) among the modern methods of assessing the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad. The BSC allows you to identify and disclose a limited number of key indicators, regularly analyzing which representative offices will be able to formulate a reasonable opinion about the effectiveness of their own activities. An important advantage of using this tool for determining the effectiveness of the activities of foreign representative offices of domestic organizations is the opportunity to find the optimal combination of estimated indicators in terms of quantity and composition, as well as identify in a single pool of indicators both traditional financial indicators based on historical data and forecast parameters [2-5]. The foreign representation of the business entity of the Russian Federation can apply the BSC to solve the following task as presented in Figure 1.
So, the key role in applying the Balanced Scorecard methodology to determining the effectiveness of the activities of representative offices of Russian business entities abroad is assigned to optimize a set of indicators, which should include both deferred and leading indicators. Reflecting the general goal of the representative office, which is increasing profits, the financial perspective can be disclosed through the traditional indicators of liquidity and financial stability, as well as reflecting the dynamics of the main indicators of the financial statements of the representative office for the past three to five reporting periods. In the composition of the financial outlook indicators, a number of authors [2] also proposes to use the economic value added indicator (EVA), the share of foreign sales in the total sales of the organization, indicators of investment in R&D, and indicators of the probability of bankruptcy. In addition to sales dynamics, in the customer perspective, indicators recommended for analysis may include the level of defectiveness of sold products, the percentage of the delivery schedule, as well as the share of new products in the total sales of the representative office. It is recommended to include indicators of labor productivity per employee, availability of alternative suppliers, compliance with the standards of the stocks of the commodity values and finished products in the list of indicators that reflects the development of business processes. Perspective indicators for sustainable growth and development of the Balanced Scorecard representation focus on reflecting the level of staff motivation to achieve strategic goals, in particular, the number of training hours per employee, the percentage of workers covered by vocational training, operating costs for an information system, and etc. [2] It is noteworthy to mention the possible limitations in applying balanced scorecard to determine the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad. Firstly, the modern approaches to assessing the effectiveness of the organization’s activities suggest a gradual shift of emphasis from a predominantly financial aspect to non-financial indicators that cover both the internal and external environment of the organization, including social and environmental factors of activity. Despite the inclusion in the scope of measurement and customer perspective assessment, business processes, and sustainable growth and learning, the method of balanced indicators mainly focuses on indicators of financial perspective, since the main indicators of achieving strategic goals are the implementation of financial goals such as the achievement of profit target values, maximization of the created added value for owner, and etc. Certainly, ensuring economic feasibility is the key task of the majority of representative offices of the Russian companies abroad. However, close attention to non-financial factors, such as the influence of the representative offices’ activities on the environment and social well-being in the region of presence, in fact, becomes mandatory to those offices that are aimed at the long-term successful operations in countries with developed market economies. Secondly, the Balanced Scorecard as a management tool and methodology for the assessment of the effectiveness of activities, in the first place and greater extent, responds to information requests of owners and managers of the analyzed representative office abroad and the economic entity itself. However, the modern management technologies based on the stakeholder approach to managing an organization imply the possibility of ensuring the organization’s long-term sustainable organization development only based on accounting and balanced satisfaction of the requests of all key groups of stakeholders, including resource and capital providers, local communities in the territory of presence, public
associations, and etc. The balanced scorecard method allows to identify and analyze the interests of key stakeholders only within the framework of four perspectives, that is, only employees, consumers, managers, and owners. So, the elements of the balanced scorecard methodology can be used for a comprehensive solution to the problem of determining the effectiveness of the activities of representative offices of economic entities of the Russian Federation abroad. However, a more complete assessment methodology is required, which is able to reflect the interests of the main groups of stakeholders, as well as non-financial aspects of the activities of the foreign representative office in the territory of presence, i.e. country and region of its actual location. As a part of modern methods of assessing the effectiveness of commercial organizations, which can be used to determine the effectiveness of the activities of representative offices of the Russian business entities abroad, it is important to note an approach based on an analysis of six types of organization’s capital allocated in accordance with the International Integrated Reporting Standard [6]. This standard prescribes to reflect on the availability, status and efficiency of the organization in public reporting using the following types of capital, such as financial, industrial (production), natural, intellectual, human and social, and network (socio-reputational). A brief characteristic of each of the six types of capital is presented in Table 1 [7].

<table>
<thead>
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<th>Table 1. Characteristic of the six types of capital</th>
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<tr>
<td>Characteristic</td>
</tr>
<tr>
<td>1 Financial</td>
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<tr>
<td>Funds of investors and lenders invested in the organization for the long-term</td>
</tr>
<tr>
<td>2 Industrial</td>
</tr>
<tr>
<td>Means of production directly involved in the organization’s operation</td>
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<tr>
<td>3 Natural</td>
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<tr>
<td>Renewable and non-renewable natural resources used in the economic activities of the organization</td>
</tr>
<tr>
<td>4 Intellectual</td>
</tr>
<tr>
<td>The complex of identifiable (intellectual property) and non-identifiable (organizational capital) intangible assets of the organization</td>
</tr>
<tr>
<td>5 Human</td>
</tr>
<tr>
<td>The complex of knowledge, experience, skills, professional qualifications of the organization’s employees, their capabilities and motivations in achieving the strategic goals of the business</td>
</tr>
<tr>
<td>6 Socio-reputational</td>
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<tr>
<td>Positive reputation of the organization in the society and business environment, social relations with suppliers, consumers, partners, organization’s employees, regulatory authorities, and etc.</td>
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It is noteworthy to mention that in accordance with the concept of integrated reporting, the organization has all the types of capital; however, their priority for management and analysis, as well as the degree of disclosure in reports, is determined by the sectoral affiliation of the organization, the profile of its activities, and etc. The organization can interpret certain types of capital in accordance with its own vision.

III. RESULTS

The approach to assessing the performance of representative offices of the Russian business entities abroad based on the analysis of six types of capital has an advantage over traditional approaches because it allows giving a comprehensive assessment of the effectiveness of the use both tangible and intangible resources of the representative office. In addition to the financial indicators, it also discloses a wide range of non-financial aspects of the activity, which actualizes this methodology in accordance with the modern requirements for disclosure of information about the effectiveness of the activities that are characterized of countries with developed market economies. This advantage is realized primarily through the proposed system of indicators of disclosing information about each of the six types of capital. In particular:

1. Analysis of the organization’s financial capital assumes the use of structure’s indicators of the invested capital, the cost of its individual sources, financial leverage, debt load, the dynamics of financial results, and dividend policy. The indicators of the weighted average cost of invested capital (WACC), the fundamental value of the business, and various profitability indicators (ROIC, ROE) can be used as aggregates.

2. The production capacity can be analyzed through the indicators of the efficiency of use of representation’s fixed assets (including energy efficiency), indicators of the dynamics and structure of fixed assets, coefficients of its movement and condition, as well as investments in capacity expansion. The production capacity and the level of its use act as a key indicator for the assessment of productive capital.

3. For the analysis of natural capital, applicable indicators reflect the use of natural resources such as water, air, mineral resources, and etc, as well as environmental impact indicators, such as emissions, discharges and waste per unit of production, and environmental investments.

4. The analysis of intellectual capital in part of intellectual property can be carried out through indicators of the structure, dynamics, condition and efficiency of the use of intellectual property in part of organizational capital.
through the quantitative and qualitative characteristics of its individual components: procedures, technologies, software, corporate culture, business models, and etc. The indicators of the share of innovative and new products in the revenue, as well as additional profits obtained by the representation through the use of intellectual capital also can be used in the analysis of intellectual capital.

5. The key indicators for the analysis of human capital are the size and dynamics of investment in human capital, indicators of health and industrial safety of workers, the level of salary and its differentiation, indicators of staff movement, and the level of its loyalty and motivation. Labor productivity is a generalized indicator of human capital.

6. By maintaining the reputation of a reliable partner, the socio-reputational capital provides an opportunity of reducing transaction costs when interacting with the suppliers, customers, personnel, regulatory authorities, and even competitors. Therefore, customer base stability and satisfaction, the share of the largest suppliers in the total volume of purchases and their reliability, standards of social support for the employees, and the dynamics of social investments can be considered as key indicators for the analysis [5, 7, 15, 16].

I. DISCUSSION

The final stage of determining the effectiveness of the representation based on the analysis of the six types of capital implies an assessment of the change in the value of each of the selected types of capital for the analyzed period. The final stage is complete by means of the analysis of the dynamics of relevant aggregated indicators and assessment of the impact of changes in this value on the primary factors of creating the value of the organization, return on invested capital, the weighted average cost and steady growth rate of capital, and the fundamental value of the organization. At the same time, an increase in the fundamental value of the business over the analyzed period is estimated as a positive outcome and a reduction in the fundamental value as a negative result of the period. This fully corresponds to the logic of the modern management approach, which is known as VBM (Value Based Management). This approach defines the main business goal, which is value creation and increment. As aggregated indicators of the organization’s performance, it is necessary to use such indicators of value creation as economic value added (EVA), market value added (MVA), shareholder value added (SVA), cash return on investment (CFROI), and etc [9]. The matrix approach to the formation and disclosure of the organizational resource information designed to structure the process of development and justification of the selection of key indicators is applied in the development of the above business performance assessment methodology [8, 18, 19]. The basic matrix that is reflecting the process of building a system of the formation and efficiency indicators of six types of capital can be presented as follows in Table 2 [8].

<table>
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<tr>
<th>Capital type</th>
<th>Resource</th>
<th>Business process</th>
<th>Results</th>
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<tbody>
<tr>
<td>Financial</td>
<td></td>
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<tr>
<td>Industrial</td>
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<td>Natural</td>
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<td>Human</td>
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<td>Intellectual</td>
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<tr>
<td>Socio-reputational</td>
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This presentation of information allows grouping the indicators of the assessment of the effectiveness of the representative offices according to the interests of certain groups of stakeholders. This analysis of the matrix makes it possible to assess the integrity and balance of individual stages of the organization’s value creation. This information allows managers and business owners to make effective management decisions. So, the method of determining the effectiveness of the representative office activities of the Russian economic entities abroad, based on the analysis and assessment of the cost of six capital types, including the use of the matrix approach, allows the development of comprehensive system of indicators that reflects the process of formation and use of main types of capital of the representative offices within the existing business models. Based on this system, it is possible to assess the performance of the representative offices in terms of creating business value, as well as to justify the most important areas of management impact to achieve the strategic goals. Moreover, due to the inclusion of the intangible types of capital in the analysis, this approach takes into account the interests of a wider range of stakeholders and makes sure to satisfy their information requests. It also affects the aspects of social and environmental consequences of the representative office activities in the region of presence through the disclosure of human, socio-reputational, and natural capital indicators. However, certain underdevelopment of methods of accounting and analysis of intangible types of capital, the incomplete methodological base of integrated reporting, the data incompatibility on the intangible capital types of various organizations make it difficult to use this methodology for determining the effectiveness of the representative office activities of the Russian business entities abroad. Another limitation, in this case, is the risk of public disclosure of information, which is a commercial secret, when reflecting information on intangible types of capital in public reporting; in particular, the organizational and socio-reputational. The above brief overview of modern techniques highlights the following aspects, which should be reflected in the updated methodology:

Firstly, the methodology for determining the activities of the Russian representative offices abroad must take into account the features and limitations of the legal field of the country, in which this or that representation operates. These restrictions are individual depending on the specific territory or region. However, if these restrictions directly or
indirectly affect the calculated values of the selected performance indicators, then such an impact should be leveled by refining the method of calculating a specific indicator or taken into account when approving its target value;

– Secondly, this methodology should be based on the stakeholder approach, which nowadays is considered as a strategic management tool for the long-term sustainability of the organization. Stakeholders can be an individual or a group of people who have the ability to influence the organization’s activities or be influenced by the organization [10]. A universal list of stakeholders for every organization doesn’t exist, just as it doesn’t exist on an ongoing basis for a particular organization because there are various changes in the strategy or business model of the organization, and in the external environment that may lead to the emergence of new groups of stakeholders or changes in the distribution of their significance [10]. That is why this methodology shouldn’t be built around a fixed group of stakeholders but should contain, as a basic principle, a mechanism for selecting KPIs to satisfy relevant information requests from the key stakeholders, which requires an ongoing dialogue with them;

– Thirdly, the up-to-date methodology should contain a balanced set of indicators in terms of the number of financial and non-financial indicators. This condition is supported by the following arguments: the goal-setting based solely on financial indicators is usually of short-term and often do not reflect the long-term consequences of the decisions made, which is equally true for the performance indicators of the investment projects). Additionally, the cost indicators are not able to reflect many non-financial phenomena and processes occurring in both the internal and external business environment and are of fundamental importance for the long-term sustainable development of business. In most cases, the financial indicators are calculated on the basis of historical data while the advanced management KPIs play an important role in the process of making effective management decisions. The reliability of these financial indicators is determined by the accounting policies of the organization and the quality of preparation of financial statements. Finally, the use of only financial indicators doesn’t allow the creation of full-fledged information space for making timely management decisions and build a truly effective business model;

– Fourthly, the modern method of determining the effectiveness of the activities of the Russian representative offices of business entities abroad should reflect the results and consequences of the activities of the representative office in the areas of presence in the context of social and environmental aspects. In most developed economies of the world, such requirements are legally enshrined. In particular, in EU countries, the relevant Non-financial Reporting Directive 2014/95 / UE dated by 22.10.2014 is in force, which determines the obligation to reflect information on sustainable development factors and associated risks in order to meet the information needs of stakeholders. Nowadays, all EU member states reflected the provision of the Directive in their national laws taking into account the specifics of each country requirements that are primarily related to the issues of the type, size, and scope of companies’ activities that must provide information in accordance with with the Directive [11, 12]. In the US, there is national standard SASB (Sustainability Accounting Standards Board) that require the disclosure of relevant information by companies, whose shares are listed in the American Stock Exchange. In the Russian Federation, the concept of development of public non-financial reporting No. 876-p. is implemented and approved by the decree of the Government of the Russian Federation of 05.05.2017 [13]. Let’s take into consideration the main elements of this methodology based on the selected key aspects [19-23]. The stakeholder approach to business management assumes that major stakeholder groups, interacting or conflicting with both the organization and among themselves, directly affect the long-term sustainability of this organization [9]. Moreover, this influence has a multidirectional effect, which can lead to either an increase in the value created by the organization or to its destruction. That is why the first stage of the methodology for determining the effectiveness of representative offices of business entities of the Russian Federation abroad involves the analysis of stakeholders, assessment of the extent and direction of their influence, as well as identification of information requests, expectations and requirements of each of the key stakeholders. As it was mentioned above, there is no universal list of stakeholders for the organization. However, there are several major stakeholders who potentially benefit from the activities and with whom the majority of representative offices of Russian business entities abroad interacts:

– Owners of the organization (representative office)
– Buyers of products (services)
– Resource providers
– Employees and employers of representation
– Financial and insurance companies
– Local communities
– Community groups and organizations
– State institutions of the Russian Federation
– State in which the representation operates, its legislative and regulatory institutions
– Business partners and etc.

The current structure of Russian exports mainly determines the activities of foreign representative offices of domestic economic entities. The purpose of the large business is to strengthen the existing production chains as a part of technological cycles through the creation of horizontally and vertically integrated holdings and to ensure the expansion of sales markets and uninterrupted supply of necessary equipment and components that are not manufactured in the Russian Federation. Such involvement of Russian business in global value chains certainly contributes to its overall effectiveness; however, it seems somewhat one-sided and devoid of a strategic vector for global diversification. In the context of globalization of the world economy, it is necessary to take into account that the cost is created not as much at the stage of production or extraction of the product as on the subsequent links of the value chain in terms of promotion, distribution and delivery, after-sales service, and etc.
Expansion of the strategic goals and objectives of the activities of representative offices of Russian economic entities abroad to the scale of the entire value chain of the relevant product will enhance the overall business performance through synergy arising from the optimization of various links in a single chain. Another important factor capable of improving the activities of economic entities of the Russian Federation abroad is overcoming the negative image of Russian business that has developed in recent years in a number of countries for various historical and political reasons. In particular, there is a high level of risk and artificial limitations for foreign investors and consumers when interacting with a number of Russian businessmen. Leaving out the political aspect, it should be noted that the key focus, in this case, is to increase the informational transparency and openness of the representative offices of Russian business entities, to demonstrate their readiness for dialogue with a wide range of stakeholders. Publishing non-financial reporting on a regular basis, creating channels of interaction with key stakeholders, and paying close attention to the environmental and social aspects of its activities will help create a positive image of the representations of Russian economic entities abroad.

II. CONCLUSION

In conclusion, it should be noted that a feature of the functioning of representative offices of domestic organizations abroad is that their activities are regulated by both the legislation of the Russian Federation and the legislation of the country in which they operate, as well as international treaties concluded between the Russian Federation and this country. Accordingly, as part of the key stakeholders of the representative office, it is necessary to single out both the state institutions of the Russian Federation and the state institutions of the country in which this representation operates.

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