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## VALUATION OF TANGIBLE FIXED ASSETS

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### ABSTRACT :

*Every business entity is forced to value its assets for different purposes. Fixed assets can be tangible like the ones mentioned above and capital work-in-progress, that is, fixed assets under construction / installation as well as intangible such as goodwill and brand. The discussion in this chapter is with reference to tangible fixed assets. An entity has the option of revaluing its tangible fixed assets. However, where such a policy is adopted it should be applied consistently to all tangible fixed assets of the same class. Where a tangible fixed asset is revalued its carrying amount should be its current value at the balance sheet date. Generally this requirement is achieved by performing a full valuation at least every five years and an interim valuation in year, with an interim valuation in the intervening years where it is likely that there has been a material change in value. Alternatively, for a portfolio of non-specialised properties, a full valuation may be performed on a rolling basis over a five-year cycle, together with an interim valuation on the remaining portfolio where it is likely that there has been a material change in value. For tangible fixed assets other than properties where there is an active second-hand market or appropriate indices, such that the entity's directors can establish the asset's value with reasonable reliability, an annual revaluation by the directors may be sufficient, without necessarily using the services of a qualified valuer. Revaluation gains are recognised in the statement of total recognised gains and losses except to the extent that they reverse revaluation losses on the same asset that were previously recognised in the profit and loss account, in which case they, too, should be recognized in the profit and loss account, after adjusting for subsequent depreciation.*

**KEY WORDS : Tangible Fixed Assets, Business Entity, Measurement, manufacturing Company, Business Operations.**

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### INTRODUCTION

Fixed assets, such as land, building, plant and machinery, vehicles, furniture and fixtures, and equipment's are the assets that enable a company reach the stage where it is ready to carry out its business operations. For example, in the case of manufacturing companies, these assets enable them to produce goods and provide marketing and administrative support to the business operations. Thus, they lead to the generation of operational revenue, which speaks of their crucial importance. In the case of manufacturing companies, they generally command the lion's share of the total assets.

Fixed assets can be tangible like the ones mentioned above and capital work-in-progress, that is, fixed assets under construction / installation as well as

intangible such as goodwill and brand. The discussion in this chapter is with reference to tangible fixed assets.

The ICAI has issued Accounting Standard (AS-10) 'Accounting for Fixed Assets', which defines fixed assets, sets out their significance, specifies the fixed assets excluded from its scope and coverage and prescribes the principles and norms of standard accounting treatment for various aspects of fixed assets valuation and accounting, i.e., identification, measurement, valuation, revaluation, retirements and disposals and disclosure requirements in financial statements prepared on historical cost basis, including revaluation. Let us discuss, understand and analyse these.

Fixed assets represent assets held with the intention of being used for the

purpose of producing or providing goods or services and are not held for sale in the normal course of business. Any expenditure that meets these criteria is identified and recognized as a fixed asset in the financial statements. And if the fixed asset has a physical existence it is classified as tangible fixed asset.

These assets play a very important role in the measurement and presentation of performance and financial position as : fixed assets often comprise a significant portion of the total assets of an enterprise and therefore are important in the presentation, assessment and evaluation of its financial position and strength. Hence, the need for proper recognition and measurement of an expense as a fixed asset.

#### **CONCEPTUAL BACKGROUND :**

The currently ongoing process of globalization and thus the deepening of mutual interactions between and among the international economies significantly affect the directions of development of accounting. The confrontation of the diverse principles of financial accounting applied in various countries demonstrates their need to harmonize them at the international level in order to achieve more extensive comparability and transparency of financial statements. However, in spite of the gradual introduction of the principles set at the international level into the national systems, in many cases there have been still a lot of discrepancies between and among the specified regulations. The objective of the study refers to the interpretation of the international standards in the scope of the initial valuation of tangible fixed asset items and the comparative analysis with the requirements. It will demonstrate both the similarities and differences between the specified acts which entail some adjustments to be made at the moment of changing the applied regulations.

A leading worldwide beverage company was planning to acquire their international supply chain. We helped the

company and its board to understand the possible depreciation effects to their Day 1 P&L as well as the accounting and valuation challenges they would need to address after the deal closed. To support our recommendations, PwC's valuation analysis combined our deep industry experience and library of cost information to provide our client with a supportable estimate of value.

A global manufacturer of construction and "do it yourself" power tools and accessories had just completed a strategic acquisition. We worked with our international network of colleagues to value more than 30 plant locations in five countries in a matter of weeks. After the initial valuation, we worked with the client to implement the valuation results into their accounting system and make recommendations for remaining depreciable lives. For a similar project, we also leveraged our analysis in allocating interest expense as part of the client's Section 861 tax assessment to help improve the company's tax position.

Accounting and tax estimates are under more scrutiny than ever. Auditors, tax authorities, courts and regulators are likely to review the methodology and credentials of those performing tangible asset valuation. Will your approach stand up to regulator and auditor scrutiny? Most accounting systems are not. Do you know what your fixed asset registers contain? Over time, events such as prior acquisitions, mass capitalizations, re-valuations, and asset transfers can impair the accuracy and transparency of your fixed asset ledgers. A quality valuation depends on deep understanding and insight of the underlying asset base.

#### **OBJECTIVES OF THE RESEARCH STUDY :**

The said research study was carried out with following objectives in view:-

1. To study conceptual background of Valuation of Tangible Fixed Assets.

2. To study the Revaluation of Fixed Assets.
3. To study the Valuation Methods of Fixed Assets.

**HYPOTHESIS :**

The main hypothesis of the said research paper is as follows:

**H 1** Every business entity is forced to value its assets for different purposes.

**H 2** Tangible fixed assets will continue to be recognised initially at their cost.

**RESEARCH METHODOLOGY :**

With the above objectives keep in mind the instructed Interview Method and Desk Research Method was basically adopted. The Secondary Data is collected from various reference books related to Tangible Fixed Assets, Financial Accounting for Management, Valuation of Fixed Assets, Commerce & Management and Marketing & Finance etc. For said research study secondary data is also collected from the National and International Research Journals which are related to Commerce, Management, Marketing and Fixed Assets.

**REVALUATION OF FIXED ASSETS :**

Sometimes financial statements prepared on the historical cost basis include part or all the fixed assets at a valuation that substitutes their historical costs, and depreciation is accordingly calculated on revalued amounts. The following principles govern the treatment of revaluation and other incidental matters.

Different bases of revaluation are sometimes used to determine the book value of the separate items within each of the categories of fixed assets or for the different categories of fixed assets. The most preferred method of restating fixed assets is appraisal by competent valuers. Indexation with general or specific price indices and reference to current prices are the other methods sometimes used. Revaluation arrived at through these methods is periodically cross-checked with appraisal method revaluation.

The revalued amounts of fixed assets are presented in financial statements by restating both the gross book value and accumulated depreciation so as give a net book value equal to the net revalued amount.

When a fixed asset is revalued, an entire class should be revalued, or the selection of assets for revaluation should be made on a systematic basis, for example, a whole class of assets in a plant. The revaluation of a class of fixed assets should not result in the net book value of that class being greater than the recoverable amount of assets of that class. An increase in net book values arising on revaluation of fixed assets is credited directly to owner's interests under the heading revaluation reserves and is regarded as not available for distribution. At times, an increase to be recorded is a reversal of a previous decrease arising on revaluation which has been charged to the profit and loss statement, in which case the increase is credited to profit and loss account to the extent that it offsets the previously recorded decrease. A decrease on revaluation is charged to the profit and loss account unless it reverses a corresponding amount in the revaluation reserve if it is considered to be related to a previous increase on revaluation.

In the case of fixed assets acquired on hire purchase terms, although legal ownership does not vest in the enterprise, such assets are recorded at their cash value, which, if not readily available, is calculated by assuming an appropriate rate of interest. They are shown in the balance sheet with an appropriate narration to indicate that the enterprise does not have full ownership thereof.

Where an enterprise owns fixed assets jointly with others (otherwise than as a partner in a firm), the extent of its share in such assets, and the proportion in the original cost, accumulated depreciation and written down value are stated in the balance sheet. Alternatively, the pro rata cost of such jointly owned assets is

grouped together with similar fully owned assets. Details of such jointly owned assets are indicated separately in the fixed assets register. Where several assets are purchased for a consolidated price, the consideration is apportioned to the various assets on a fair basis as determined by competent valuers.

### **FIXED ASSETS VALUATION METHODS**

Some fixed assets valuation methods are used for various purposes of valuation, such as financial accounting, tax purposes, but also above mentioned valuation for fixed assets purposes. Such methods shall be included:

#### **1. Valuation based on replacement cost basis:**

In this case, it is determined the cost of a new asset of the same nature, design and capacity. These costs represent the base value of the replacement cost.

#### **2. "Good as new":**

There are situations where plants and machinery operates satisfactorily thanks to proper maintenance. In these cases are applied valuation methods, which represent the actual original cost less depreciation, but with the addition of maintenance costs.

#### **3. Sum of part valuation:**

This method is used when the device has not a composite character. In this method, all the different parts/components are measured separately and then added together to form a composite value. This method has disadvantage of the technological process in the sense, that if one part is damaged or not available, the whole assembly becomes unusable. Loss in such a situation is not just concerned to that particular part.

#### **4. Fair value method:**

This method is used for the valuation of assets, which can currently be exchanged in the market for some part exchange.

#### **5. Depreciation method:**

**a. Book value:** represents the written down value of the asset in the book of accounts. In the first year, this represents a real cost of asset. With each passing year corresponding depreciation are attributed and the asset value is reduced accordingly. Sometime the value of the asset is so low that it will not represent the actual value of the asset.

**b. Market value:** this method allows depreciating the current replacement value of assets during the years of operation, unless it comes to market value.

### **CONCLUSION :**

Tangible fixed assets will continue to be recognised initially at their cost. However, there is a new criterion for recognition that it is probable (more likely than not) that there will be an inflow of economic benefits from the asset. The valuation basis has also changed slightly. Land and buildings will now be valued at fair value, not open market value on an existing use basis. This will affect the valuation of certain assets where redevelopment will significantly change their value. Specialised properties can continue to use the depreciated replacement cost basis. The business is, in terms of the total capital invested, defined as a functional combination of all its related assets (property), which include tangible assets (real estate – buildings, plant, machinery and supplies), intangible assets and working capital (difference between current assets and current liabilities). These assets are valued separately for different purposes and one of them is the valuation for insurance purposes. In monographs we encounter a variety of valuation methods of fixed assets, but the choice of the appropriate method depends mainly on the nature of the asset itself and the expert who valued assets. That determines and decides which method is most suitable for the valuation of a particular asset.

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