PART II: ACTUAL ISSUES OF MACRO- AND MICROECONOMICS

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CORPORATE STRUCTURES AND THEIR IMPACT ON DEVELOPMENT OF BOOKKEEPING AND ACCOUNTING

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***Abstract**: A long-standing ideology in business education has been that a corporation is run for the sole interest of its shareholders. Corporations are now engaging in environmental and social causes with multiple stakeholders in mind. The article attributes this phenomenon to the increasing concentration of economic activity in the world's largest corporations, which has led to a larger social and environmental impact from the activities of few corporations that can be more easily located and held accountable by an increasingly activist civil society. The article also presents a corporate structures and their impact on development of bookkeeping and accounting. Specifically, we encourage for research on the materiality of environmental and social issues for the future financial performance of corporations, the design of incentive and control systems to guide strategy execution, corporate reporting, and the role of investors in this new paradigm.*

***Keywords**: corporation, impact, accounting, corporate structures, holding companies, shareholders, corporate relations*

INTRODUCTION

The sustainable growth of the Gross Domestic Product and improvement of the investment environment give evidence of the positive dynamics in the socio-economic development of Ukraine, strengthening of market relations and stabilization of the domestic economy. To a large extent, it comes out of the operating efficiency of corporations, as well as their business, financial and investment activities. Nowadays, the corporate structures become consolidation centers of property and integration of capital in Ukraine.

The aim of the article is to explore definitions of corporations that will allow conclusion that these definitions contain a number of formal features: (1) voluntary association of legal entities and individual proprietorships for entrepreneurial activity; wide range of activities; (2) developed system of economic relations; (3) professional staff; (4) activity based on the national legislation. It creates a need to collect, record, analyze information about corporative formation.

The main tasks of our research are: (1) scientific review of the definitions of corporations; (2) investigation of corporation advantages and disadvantages; (3) discovering of the corporative structures impact on development of accounting.

MATERIALS AND METHODS

From the Adam Smith's time, through the age of industrialization, the Great Depression, and the recent half-century of globalization and prosperity, the purpose and role of the business enterprise (viz. the large corporation) has been the focus of debate. Some governments have attempted to tame the corporation through regulation. Others have taken major spheres of economic activity into the public sector, often with unsatisfactory results and subsequent privatization. Whatever the terms of debate, the fundamental questions remain the same: What is the corporation and to whom and for what are it and its managers responsible? The corporate form originated in medieval times, when governments to grant special institutional status to cities, religious institutions, and universities used it. During the XVIII-XIX centuries, business corporations were increasingly chartered in North America and Europe, typically in order to pursue narrow purposes, viz. financing ocean voyages and building canals, turnpikes or railroads. By the XX century, governments in many countries were granting corporate charters with broad and general purposes, such as "to carry on business for a profit". As a result, corporations operating within market-oriented environments became free to pursue almost any legal business activity and to change their purposes, activities and organizational structures. Freedom of action is limited for corporations operating within authoritarian settings. However, the scope of market processes has been widening globally and the extent of government control over business correspondingly declining, and this trend is expected to continue.

Let us consider definitions of the term *corporation* from various sources for correct interpretation and full understanding. The explanatory dictionary of the Russian language defines the corporation as a community, a society, an association, a partnership, a social category, a union of people of the same rank or mechanical and industrial arts. F. Brokgauz & I. Efron (2002) understand *corporation* as a common name for many types of unions that have an internal organization rallying the members of the union into a single whole, being the subject of rights and obligations, a legal entity. In the modern dictionary of the Russian language (1991), a corporation is (1) a united group, a set of people of the same profession and the same social category; (2) one of the forms of monopoly association. The large commercial dictionary (1996) defines a corporation as a form of entrepreneurship administration widely used in developed countries, providing for the equity ownership, legal status and concentration of management functions in hands of the employed professional chief executive officers (managers). Corporations can be both public and private. The legal status of corporations determines the system of profit taxation. According to the foreign vocabulary, a corporation is a society, an alliance, a group of persons united by the communion of professional or class interests (1964). The Explanatory Dictionary of Terms for Corporate Relations and Securities (1994) offers the broadest definition of the term *corporation* as a legal entity registered by a state governing body and acting in its individual capacity separately from its owners. The corporation can own property, have debts, institute court proceedings or be subjected to persecution. It has three main features: (1) limited liability (corporation is liable for debts with its own property, i.e. the owners can lose only what they have invested in the corporation);

(2) simple transfer of ownership by the sale of shares; (3) specified period of existence (it may be unlimited). Nowadays in economics and legal literature corporation is identified as the economic category. Open joint-stock companies or corporations are the highest form of capital flow, the advantage of which is in the adequateness of corporate property to the regulatory and market mechanisms of the mixed society economy (Andronov, 2003). Foreign specialists in the area of corporate relations note that "a corporation is an association of persons having certain rights, privileges and obligations appropriate for an independent economic entity, distinct from the rights, privileges and obligations inherent to each member of a corporation taken separately" (Chernyshov, 2000). P. Stepanov (1999) considers *corporation* (from the Latin *"corpus habere"*) that denotes the rights of a legal personality. Other authors consider corporation (from the Latin *"corporatio"*) as the union. J. Van Horn (2000) defines a corporation as an impersonal enterprise created by law allowed to own assets and incur liabilities. A number of authors consider a corporation as an association of several legal entities that do not have the status of a legal entity. Yu. Vinslav (2001) noted that in most cases the modern large corporation appears as a set of legal entities that jointly accomplish common purposes and interests. I. Mazur et al (2005) contain the extensive definition of a corporation. A corporation means a profit oriented business (legal entity including joint-stock company and other types of business entities) having developed organization structure; wide range of activities (developed system of strategic economic zones) or a limited range of activities, but occupying a significant position in the relevant market); developed system of economic relations; professional staff. V. Andronov (2003) defines modern corporations as large enterprises and associations, where business entities voluntarily pooled their resources in the consolidated capital and created the system of management based on free division of labor and cooperation, as well as common strategy for the purpose of sustainable acquisition of entrepreneurial income. E. Novitskij (1999) considers the corporation as a group of legally or economically independent enterprises (entities) engaged in the joint activities based on consolidation of assets or contractual relations in order to achieve common purposes. A big bookkeeping dictionary defines a corporation as a form of entrepreneurship administration widely used in developed countries, providing for the equity ownership, legal status and concentration of management functions in hands of professional chief executive officers. Corporations can be both public and private. The legal status of corporations determines the system of profit taxation. V. Grey & B. Nidls (2006) emphasize that the corporation differs from other forms of organization by the fact that it is legally separated from its owners (shareholders). Shareholders, whose property is represented by shares, do not exercise direct control over the corporation activities. They elect a Board of Directors to manage the corporation for their own benefit. Notwithstanding the fact that the number of corporations is less than the number of individual proprietorships and partnerships, they contribute much more to the economy in monetary terms.

We can conclude that corporation is: (1) association of persons, who joined forces to achieve common goals, conduct joint activities and establish a separate legal subject, i.e. legal entity; (2) joint-stock company with a multidivisional structure; (3) type of

international economic cooperation evident as creation of international corporations; (4) separate joint venture company established by the companies from different countries; (5) creation by means of acquisition of the controlling parcel of shares in a foreign company by the national company; (6) creation by means of amalgamation of companies from different countries; (7) acquisition of the national companies by the foreign corporation. Abovementioned definitions allow underlining such formal features as: (1) voluntary association of legal entities and sole proprietorships established to carry out entrepreneurial activities; (2) wide range of activities; (3) developed system of economic relations; (4) professional staff; (5) activities based on the national legislation.

RESULTS

The corporate property acts as the social and economic basis of the corporation. The main features of the corporate property are: integrated property of economically self-supporting entities that voluntarily pooled their individual capitals in order to ensure sustainable production on the innovative basis; corporate property that denies the personal appropriation of production means by the owner, which is the associative property of the various owners of capital, labor and entrepreneurship within the framework of a corporate association. As a rule, the legal organizational form of such associative property is an open joint-stock company. The Law of Ukraine "On Joint - stock companies" governs the activities of Ukrainian joint - stock companies (2008). Corporations are also consolidated groups of entities formed as a result of intra-industry and inter-industry capital flow. Modern market economy is presented by large industrial corporations or financial and industrial groups, which sphere of interests is not only the resources pooling and receiving profit, but also the use of advanced technologies, application of modern equipment, mobilization of financial resources and productive diversification. Financial and industrial groups are distinct in the forms of industrial integration, sectoral affiliation, spheres of activity (national, regional, international) and diversification degree. They combine industrial, financial, commercial and banking capital under the responsibility of the central leading company. The principal company of the financial and industrial group forms various entities that are full members of the share capital and manages a multifaceted cycle – from production, management, financial support to the sale of products in the domestic and foreign markets. Law of Ukraine "On financial and industrial groups in Ukraine" (became invalid in October 02, 2010) defined financial and economic conditions for their activities. Nowadays Law of Ukraine "On Holding Companies in Ukraine" (2006) is the holding model basis, as a holding company is organized as a joint-stock company, which owns, uses and manages the holding corporate shares (participatory interest or equity interest) of two or more corporate enterprises.

The internationalization of production and productive forces development have contributed to the emergence of transnational corporations, i.e. enterprises that own or control the industrial complexes or services sectors located outside the national territory, where these corporations are based (in Ukraine transnational corporations are regulated by the Convention for Transnational Corporations (1998)).

Transnational corporations (*TNC*) are active centers of economic globalization. They operate in different countries regardless of national boundaries and become global corporations. *TNC* link thousands of enterprises formally independent, but closely connected with them, acting as the suppliers of components, whose activity is predetermined by the concern behavior. The *TNC Concept* includes different companies at the level of concerns, holdings, financial and industrial groups and joint-stock companies. Significant production scales provided by TNC in many branches of industry ensure the economic efficiency; high production concentration provides capability for competitive activity, opportunity to reduce costs and to increase profit. *TNC* are economic associations including the parent company (holding company, mother company) and foreign subsidiaries. The parent company participates in the enterprises capital and controls participants. The trans nationalization process is typical for the modern world economy. TNC hold key positions in the productions and sales. TNC does not depend on the origin country and the ownership form; it has branch offices operating based on single policy and strategy. The *interstate corporation* operates in the territory of another country based on the agreement between the governmental authorities of the origin and another country. The *state-owned corporation* operates on a national level. Organizations registered in the territory of the same region constitute as *regional corporations*.

TNC keep a considerable part of global industrial production (0.25-0.33%), trade and banking operations. They cover about 67% of the world trade and own about 80% of the world bank of patents and licenses for innovations. E.g., in the US they own 80% of the value of all sales and 90% of all profits, while sole proprietorships and partnerships own 13% and 4% respectively and 7% and 6% respectively.

The corporations' development requires significant capital investments and pooling the capital of several owners. The need to create an adequate system of invested capital accounting, capital flow in the process of capital turnover, costs and profit assessment has promoted the development of accounting and emergence of new accountable items. Yu. Vinslav (2001) wrote that organizational and managerial relations regarding the formation and use of the share capital are the subject of corporate analysis and regulation. V. Palij & Ya. Sokolov (1988) noted that the accounting subject is a capital, as the amount of funds invested in the economic activity, movement and transformation of funds in the process of turnover. They emphasize the role of accounting in the reflection of ownership at the capital, capital division into owned capital and borrowed capital, contributed capital and accumulated capital, basic capital and floating capital, etc. At the stage of growth and maturity of corporation, the amount of internal capital can change. The capital increase is accounted for the allocation of undistributed profits of the corporation to the creation of new assets, revaluation of assets, additional issuance of shares, etc. Structural changes in the own capital is due to the capital restructuring, asset flow and buildup of reserves. The liquidation stage assumes the repayment of own shares for subsequent cancellation, reflection at the withdrawn capital and subsequent impairment of authorized capital.

The definition of the capital is absent in the domestic legal framework for the accounting, but in accordance with the National Generally Accepted Accounting

Principles (Standards), the own capital shall include authorized capital, additional capital and reserve capital, undistributed profits and other reserves. According to the concept of accounting in the market economy, the capital is considered as a balance of economic assets after deduction of creditor indebtedness, i.e. it is considered equivalent to the net asset value. According to Anthony, R. & Rees, J. (1993), the capital is also known as net assets, because the amount of internal capital is always equal to the assets after deduction of liabilities. It is just own capital, i.e. assets after deduction of liabilities. At the same time, it is impossible not to note the subjective nature of the net asset value, which depends on the valuation methods of assets and liabilities. Establishment of subsidiaries by means of acquisition of shares or ownership interest, as well as by conclusion of joint venture agreements influenced over the development of corporate bookkeeping and accounting. Associations of legally independent entities linked by the relations of economic dependence in the legislation of foreign countries are considered as groups of related companies, etc. S. Puchkova (2004) determines the consolidated group of enterprises as an association of legally independent entities, based on the acquisition of title by the parent company and control over subsidiaries and dependent undertakings. V. Plotnikov & V. Shestakova (2004) point out that the group acts as a single business entity and implements the general financial and economic policy with the aim of making profit and implementing investment projects. Law of Ukraine "On joint-stock companies" (2008) provides for the participation of joint-stock companies in business associations. Acquisition of shares and emergence of other forms of control generated a need for reflection of the charter capitals of other entities, business reputation (goodwill), minority ownerships et al in the corporate accounting and consolidated corporate reporting.

For the first time, consolidated statements were published in 1901 by the US based company *United States Steel Company*. In 1939, the London Stock Exchange for the first time demanded consolidated reporting. Consolidated report was firstly mentioned in the UK legislation in 1947, in West Germany in 1965 and in France in 1986. Elements of consolidated report combining the indicators of a subsidiary company and a holding company are business reputation (goodwill) representing the difference between the current market value and the net assets value, as well as the minority ownership reflecting in the balance sheet the amount of authorized capital and in the profit (loss) statement the amount of financial results of activity of the subsidiary company not belonging to the parent organization. Investments in the associated company and capitalized earnings (loss) value reflecting the share of the parent company in the profits (losses) of the associate company are the elements of consolidated reporting combining the indicators of affiliated company and the parent company. After conclusion of the joint venture agreement, venturers should reflect in the corporate statements jointly conducted operations, jointly controlled assets, contributions of partners to joint activities and associated economic events.

Transaction, i.e. economic event associated with the exchange of property rights, is one of the items inherent to the corporate accounting. Transaction is a key concept in modern institutional theory, which is often defined and considered as the transaction-cost-economics. Modern accounting does not consider economic

transactions as independent accounting items. However, expansion of economic relations and corporations' emergence and development intensified the need for presenting in bookkeeping the economic events associated with the entrance to the market, property rights protection, maintenance of business relations, affording access to resources, integration of entities et al. Transacting inevitably causes costs, defined as transaction expenses.

The information formed in the corporate accounting is an indicator of the agency problems resulting from the agency relations defined in the scientific literature as a contract, whereby one (or more) principal employs an agent for the provision of certain services that involves delegation of property control powers to the agent (Rudyk, 2004). It is assumed that the manager acts in the interests of shareholders and takes measures to increase the market value of shares. However, in practice, in the corporate management course often focuses on personal views of profitability and risks, which contribute to the conflicts of interest between principal and agent. Agent costs influence significantly the investment, operational and financial policies of the corporation and its value. The typology of agency problems for researchers: (1) *problem of efforts*: managers use insufficient efforts from shareholders' viewpoint; (2) *problem of the investment horizon choice*: managers will always prefer a short-term investment project to a long-term one; (3) *problem of different perception of risks*: manager's welfare directly depends on the availability of the working place and business reputation; the reputation loss depends on the riskiness of investment projects. The extent of potential losses of shareholders is limited by the amount of assets invested in the corporation, and therefore, they prefer to realize investment projects, where the risk is compensated by higher yield; (4) *problem of inefficient use of assets*: manager's welfare does not depend on the effective assets use and the current market corporation value. Advantages of the corporation structure are as follows: (1) *limited liability*; (2) *source of capital*; (3) o*wnership transfers*; (4) perpetual life. Disadvantages of a corporation are as follows: (1) *double taxation; (2) excessive tax filings*; (3) *independent management*. One of the main functional advantages of corporations is that they have the ability to raise capital for their business through the ownership interests' sale in the business in the form of stock offerings. Another functional advantage of corporations is that they are generally able to attract and hire highly qualified staff, because they tend to offer competitive benefits and the potential for partial ownership through stock options. Third functional advantage of corporations is that their ownership interests can be freely transferred (via transfers of stock shares) unless limited by the bylaws or some other agreement.

Corporations are often considered most advantageous concerning liability.

A corporation is, for all purposes, treated as a separate and distinct entity from its owners. It means that owners of a corporation (shareholders) are not liable for the debts or obligations of the corporation – if the corporation incurs large debts or obligations, the owners' assets are protected. The most that an owner/shareholder of a corporation can lose is the input amount, however, if the necessary formalities of the corporation are not maintained or if the corporation is used merely as a *front*, then owner/shareholders could lose the limitation of liability and be held personally

responsible for debts and obligations. In addition, corporations have tax advantages, i.e. they typically file taxes separately from their owners. Therefore, owners only pay taxes on the corporate profit that are actually paid to them in the form of salaries, bonuses and dividends. Functionally, corporations are costly and timely consuming to operate. Incorporating requires start-up costs, operating costs and tax costs that are not typically required to form other business entities. Furthermore, there are raised paperwork and recordkeeping duties, because corporations are highly regulated by federal, state and in some cases local agencies.

CONCLUSIONS

Globalization of entrepreneurial activities of the corporations promoted the development of the derivatives market, which was actively developed in the XX century. Making transactions with postponing of execution, standardization of contracts and the sale of associated rights and obligations gave rise to forward contracts, futures contracts, option contracts and swaps. Regulatory documents governing the accounting in Ukraine do not consider the arrangements for accounting for derivative tools. There is no definition of forward contracts, futures contracts, option contracts and swaps as accounting items. Modern economy is characterized by the significant fluctuation of prices for different types of assets and participants in the market are interested in creating protection against price changes and adverse consequences. Derivative tools give the possibility to share, limit and manage risks. The change in the accounting price of derivative products influences a company's profit (loss) and requires continuous monitoring. E.g., commodity futures and options help producers to take out insurance against the risk of price changes in the commodity markets. *TNC* hedge the risk of currency depreciation by means of forward contracts, futures contracts and option contracts. Increasing the range of possible investments choice is one of the important functions of derivative tools. The derivative market in Ukraine is on the rise generating a need for presentation of the initial cost of basic asset, valuation changes and transaction expenses associated with the asset flow in the corporate accounting.

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