

HUMAN RESOURCE ACCOUNTING IN INDIA: AN OVERVIEW

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Abstract

Human beings are the most valuable resource. Employees are the greatest asset of an organization and the success or failure depends on the skill and the performance of the employees. Almost all the large sized organizations have a separate HRD Department. Human Resource Accounting is a process of identifying and measuring data about humans resource and communicating this information to the interested parties. HRA helps the management in taking managerial decision relating to selection, lay-off, transfers, training, promotion etc.

Attempts to account the HR are not new. It was Rensis Likert who initiated research into HR accounting in the sixties and in organizations starting with the Milwanke Braves USA (1963), which was the first organization to experiment with the concept of HRA, by treating its investments in future team development as an asset to be capitalized and amortised over its expected useful life rather than as an expense in the period incurred. The concept of recognizing human being as an asset is an old one in India. Akbar gave importance to the nine jewels (courtiers). The names of freedom fighters like Mahatma Gandhi, Pandit Nehru cannot be forgotten in the history of freedom movement of India but no one made efforts to assign any monetary value to such individuals in the balance sheet of the nation. Indian Companies Act, 1956 does not provide any scope for furnishing any significant information about human resources in financial statement but a growing trend towards the measurement and reporting of human assets, some companies in public and private sector.

Optimum use of manpower is a very vital question in the survival and growth of an organization. Development of manpower is very essential to achieve better equilibrium in the organization. The nation of treating "people" as assets and Accounting them in rather logical and satisfactory as to the expectation of future economic and their measurability. It is to pointed that treating people as assets should not be considered as lowering the status

of human dignity as in the case of "slave trade". Where quite readily people bought and sold.

Human beings are the most valuable resource. Employees are the greatest assets of an organization and the success or failure depends on the skill and the performance of the employee. Almost all the large sized organization have a separate HRD department. Business organization need to understand the new conceptual framework of human resource accounting.

Human Resource Accounting is a process of indentifying and measuring data about human resource and communicating this information to the interested parties. The role of human resource in the process of managerial planning and control cannot be overemphasised. It helps the management in taking managerial decision relating to selection, lay-off transfers, training, promotion etc. There are two major resons why human resources. Accounting has been receiving so much attention in the recent years.

First, there is genuine need for reliable and complete information which can be used in improving and evaluating the management of human resources.

Second, the traditional framework of accounting is in the process of being expanded to include a much broader set of measurement than was thought possible or desirable in the past.

Development of HRA:

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any monetary value to such individual in the balance sheet of the nation.

William Petty (1991) made the first attempt to value the human beings in monetary terms. The real work was started by behavioural scientists from 1960 onward. The notable experts were Shultz (1960), William Pyle (1967), Flam Holtz, Jaggi and Lav (1974), N. Dasgupta (1978) and Dr. Rao (1983) etc. Who developed appropriate methodology and procedures for finding out the cost and value of the people to the organization.

Concept and Definition of HRA:

HRA is a new branch of accounting. It is a process of identifying and measuring data about human resources and communicating this information to the interested parties.

HRA means accounting for people as the organisational resources. It is the measurement of the cost and value of people to organizations. It is the art of valuing, recording and presenting systematically the work of human resources in the books of accounts of an organization.

Few important definition of HRA are given below:

The American Accounting Association has described HRA as “The Process of identifying and measuring data about human resources and communicating this information to interested parties”.

Stephen Knauf calls it “Human Resource accounting is the measurement and quantification of human organizational inputs such as recruiting, training, experience and communication”.

HRA according to Prof. Flamholtz “Accounting for people as an organization resource. It involves measuring the costs incurred by business firms and other organization to recruit, select, hire, train, and develop human asset. It also includes measuring the economic value of people to organization”.

The basic theory underlying the Human resources Accounting is-

- (A) That people are valuable resources of an organization.
- (B) Information on investment and value of Human Resource is useful for decision making in the organization.

The Need for HRA:

It is known fact that success of an organization depends on the quality, Calibre and character of the people working it. The need for HRA arose primarily as a result of the growing concern for human relations management – In Industry. If

accounting is to provide meaningful information about the financial state of affairs of a business unit, it must develop standards to measure the value of human resources both for financial accounting and as an aid for managerial decision making. Unfortunately, the financial statements which are the end products of financial accounting, fail to disclose any information about the most valuable asset like Human Resources. Human resources is a very valuable asset without which an organization can not progress in all directions.

In modern times, the investment in human resources is occupying a pivotal place in a business enterprise, since a well organized and loyal personnel can be considered as more valuable asset than a stock of merchandise. The balance sheet of a business concern cannot represent “a true and fair view” of its financial affairs as long as all the assets and resources including the “human resources” are not properly disclosed. HRA has a profound impact on the decision-making structure in an organization. Besides management decision-making, HRA is also needed to facilitate the effective management of an organisation’s human and material resources. Moreover, a positive correlation exists between the profit of an organization and the investment on acquisition, training and retention of human resources. Above all, the real ROI cannot be computed unless the investment in human resources is taken into consideration. In conventional accounting a major portion of costs relating to recruitment, training and development are treated as revenue expenses. But all these expenses are essentially of the nature of investment resulting benefits over a number of years.

Objectives of HRA:

The primary purpose of HRA is to facilitate the management of people as organizational resources. To generate human data about human resource, to assign value to human resource and to present human assets in the balance sheet. Following are main objectives of HRA:-

- (i) Developing, new measures of effective manpower utilisation.
- (ii) In taking decision regarding promotion, transfer, training, retirement and retrenchment of such resources.
- (iii) For fixing right person for the right job.
- (iv) To furnish cost value information for making management decision about acquiring, allocating, developing and maintaining human resources in order to attain cost effective organization objectives.

- (v) To provide a determination of assets control.
- (vi) To aid in the development of management principal by classifying the financial consequences of various practices.
- (vii) To Recognise the nature of all resources used or cultivated by a firm and improvement of the management of human resources so that the quality and quantity of goods and services are increased.
- (viii) To facilitate the effective and efficient management of human resources.

HRA also help decision making in following areas:-

- (a) Direct recruitment Vs. Promotion
- (b) Transfer Vs. Retention
- (c) Retrenchments Vs. Retention
- (d) Impact of budgetary controls of human relations and organizational behaviour.

From the above, it is clear that there are three important aspects of HRA as given below:-

- (i) Valuation of human resources.
- (ii) Recording the valuation in the book of accounts.
- (iii) Disclosure of the information in the financial statements of the business.

Methods of valuation and Accounting Human Resources:

The important methods to value for human resources can be classified into the following categories:-

- (I) Methods based on costs (which include costs incurred by the company to recruit, hire, train and develop human resource)
- (II) Methods based on economic value of human resources

(I). Methods based on Cost:

Under this main approaches method following are-

(A) Historical cost method:-

This approach was first developed by William C Pyle. Under this method, the cost of acquisition i.e. selection, hiring, training costs of employees are capitalized and written off over the expected useful life of the employees. In case, the personnel leave the company before the anticipated period of service, then the unamortised portion of costs remaining in the company's books is written off against the profit and loss account in that year. If the period of service exceeds the anticipated time, then amortisation of costs is rescheduled.

(B). Replacement cost method:-

Under this method, the human resources are valued at their replacement cost i.e. the monetary

implications of replacing existing personnel. Replacement costs could be positional i.e. replacing personnel for particular positions or personal i.e. replacing specific talent or ability of particular persons.

(C). Competitive bidding method:-

This approach suggests competitive bidding for scarce employees in an organization i.e. opportunity cost of employees linked to scarcity. The approach proposes the capitalizing of additional earning potential of each human resource within the company.

(D). Standard cost method:-

Under this method, standard costs of recurring, hiring, training and developing per grade of employees are determined annually. The cost standard cost for all personnel of the company is the value of human resources.

(II). Methods based on Economic value:

(A). Jaggi and Lau method:-

This method estimated the worth of human resources on a group-basis, as human resource group account for productivity and performance in organizations.

(B). Economic value method:-

Under this method, the net present value of incremental cash flows attributed to human resources is taken as the asset value.

Role of HRA in an organization

The success of any business unit largely depends on the intensive application of skill, creativity and dexterity of the people working therein. Eric Flanholtz defines human resources accounting as, "Accounting for people as organizational resource. Human resources accounting is measurement of the cost and value of people for organizations." It is clear from this definition that the human resources accounting is useful for both general managers and personal managers since human resources information influences the planning and controlling functions of the management and various operative function of personal management. It helps the management to utilize human resources most economically and efficiently. It also helps the managers in making sound decisions in personal matters by providing required information. HRA helps management review its strategy of investment in human assets. The accounting concept helps as certain effectiveness of the entire gamut of human resource management. HRA is of permanent importance to the nation and also to individual organizations. It is all too easy to see a company in abstract terms of balance sheets, technologies and

organization charts. Such a view overlooks the fact that the most valuable assets are the commitment and skills of individuals who make the system work and lay the foundations for future growth.

Apart from laying stress on training, companies offers a host of facilities to its employees to maintain a congenial working environment. Among those given at the factories: houses/tenements for a large number of workers and staff, cooperative societies, crèches, dispensaries/hospitals, canteens, rest halls and so on. Benefits are liberally subsidized by the company. They also care of employees' families through merit scholarship, tuition fee reimbursement, medical treatment etc. The following are the main benefits of HRA:-

- The adoption of the system of HRA discloses the value of human resources.
- Improves managerial decision making.
- Helpful in proper interretation of return on capital Employed.
- Adoption of HRA will help increating productivity of human resources.
- It will serve social purpose by identification of human resources as a valuable asset.
- HRA is absolutely essential in such organization where human element is the prime factor like – a professional accounting firm, a drama company etc.

The success of an organization very much depends on the build up of quality workforce at all levels. If this vital asset is not shown in the balance sheet, to the extent the public and investors are handicapped.

Aspects of HRA:

HRA include three steps (A) measurement and valuation of human resources (B) Recording the cost and value in the books of account and (C) Communicating the relevant information through financial statements to measurement and external users. There are two major aspects of HRA

(I). Human Resource Cost Accounting:-

HRCA is the measurement and reporting of costs incurred to acquire, develop and replace people as organizational resources.

(II). Human Resource Value Accounting:-

HRVA is the assessment and recording the value of contribution of the member to the production and the processes.

HRA in India:

Indian companies act, 1956 does not provide any scope for furnishing any significant information about human resources in financial statement.

Beyond it, there is no rigid instruction on behalf of the companies act, 1956 to attach information about the value of human resources and the result of their performance during the accounting year in notes and schedules. In company law (under section 217) only remuneration paid to employees is showing in financial statements. In India a growing trend towards the measurement and reporting of human assets, some companies in public and private sector. The following companies do give information of their human assets by following a particular model of valuation of human resources.

- (1). The Bharat Heavy Electricals Limited (BHEL) - is the largest engineering and manufacturing enterprise in India. The greatest strength of BHEL is its highly skilled and committed 42,600 employees. It was the first Indian Company to publish human resources accounts from 1974-75 onwards.
- (2). Cement Corporation of India Limited (CCI)
- (3). Oil and Natural Gas Commission (ONGC) - It uses HRA since 1994-95. Today ONGC is the flagship Company of India and making this possible is a dedicated team of nearly 40,000 professionals who tail round the clock.
- (4). The Minerals and Metals Trading Corporation (MMTC) - Established in 1963, MMTC one of the two highest foreign exchange earner for India is a leading international trading company with a turnover of over US \$ 3 billion.
- (5). Engineers India Limited (EIL) - It is ISO 9001-2000 Company. It was established in 1965 to provide engineering and related technical services for petroleum refineries and other industrial projects. The total manpower is 3000 in this company.
- (6). Oil India Limited (OIL)
- (7). Steel Authority of India Limited (SAIL) - is the leading steel-making company in India. Ranked amongst the top ten public sector companies in India in terms of turnover.
- (8). Southern Petro Chemical and Industries Corp (SPIC) - Since its founding in 1975, SPIC has been providing products and services that feed, nourish and protect the agriculture and rural eco-system.
- (9). Associated Cement Company (ACC) - It was established in 1936, total employees are 9000.
- (10). Infosys Technologies
- (11). Satyam Computer
- (12). DSQ Software - is a global company providing IT consulting and software development

services in diverse application areas. Established in 1992, it has consistently provided high-quality software solutions in a cost-effective manner and on time, to a discerning clientele worldwide.

Of the above companies, first seven companies are in the public sector and the last five are in the private sector.

These companies have followed the “present value of future earning model” of Lev and Schwartz (1971). However, CCI and ACC mention in their annual reports that they have adopted models as enunciated by Lev and Schwartz (1971). Eric Flamholtz (1974) and Jaggi and Lau (1974) with appropriate modifications. It is heartening to note that some enlightened companies in India have reported HRA in their annual reports. Since none of the organizations have mentioned the purpose for which HRA information is being used by them, it seems that their objectives of introducing HRA has been image building and they have been successful in this as BHEL, CCI and MMTC have received the awards from the ICAI for the best presented published accounts. However, this information may be significant for the investors and other external users of the financial statements. The prospective investors and lenders are interested in knowing about the organization, investment in human resources and their value to the firm for the purpose of their investment decisions.

Limitations and Problems of HRA:

HRA system has the capacity to provide the cost and the value measures of employees depending on the design of the system. HRA is very important for an organization, yet its development and application in different industries and organization has not been very encouraging. Following are main problems of HRA-

- The life of human resources is uncertain and therefore, valuing them under uncertainty seems unrealistic.
- There are no specific guidelines for finding cost and value of human resources of an organization.
- Another issue which has not been settled so far is about the rate at which the prospective stream of contributions is to be discounted to calculated its present value.
- Human resources unlike physical assets, are not capable of being owned, retained and utilized at the pleasure of the organization. Hence, treating them as “asset” in the strict sense of the term, could not be appropriate.
- Tax laws do not recognize human beings as assets. So human resources accounting has been reduced to a merely theoretical concept.

- There is a possibility that HRA may lead to dehumanizing and manipulations in employees.

Conclusion:

A survey of the annual reports of companies reveals that the chairman’s report invariably contain the statements highlighting the significance of human resource. Like – “I wish to place on record my sincere gratitude for the hard work done by the employees of our company”, “our employees are our most important assets and without their significant contribution, the present growth in operations, would not have been attained”, etc. though these qualitative statements reflect the pivotal role played by the human resources in an organization. Optimum use of manpower is a very vital question in the survival and growth of an organization. Development of manpower is very essential to achieve better equilibrium in the organization. Almost all the large sized organization have a separate HRD Department. HRA is measurement of the cost and value of people for organization and communicating this information to interested parties.

Human capital is not nearly a component of capital, it is the most critical attribute that form the basis for other form of capital. The most important is human capital, the ability of employees to do the things that ultimately make the company work and succeed. Hard to define, and ever harder to measure, intangible assets are becoming increasing essential to the success of many organization in the 21st century. In a business enterprise, a well organized and loyal personal may be much more asset than a stock of merchandise but it is unfortunate that accounts, till now, could not evolve a generally accepted system to value and record this important assets viz. Human Resource. The Nation of treating, “people” as assets and accounting them is rather logical and satisfactory as to the expectation of future economic and their measurability. It is to be pointed that treating people as assets should not be considered as lowering the status of human dignity as in the case of “Slave trade”. Where quite readily people were bought and sold.

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