Human Resource Accounting: an Implication for Managerial Decisions in Indian Hotel Industry

Mohinder Chand
Associate Professor, Department of Tourism and Hotel Management, Kurukshetra University

Heera Lal
Senior Lecturer, BPR College, Kurukshetra (HR)

Abstract:-

Hotel and tourism, with its immense employment generation capability is very often called 'people intensive industry'. In this industry, human resources constitute a higher element of total operating cost. Obviously, the effective and extensive Human Resource Management (HRM) is critically significant to control the operating cost for long run survival. The Human Resource Policies and practices of every hotel company will have direct impact on procurement costs, quality human resources, delivery of quality products \ services and reduce employees turnover. Therefore, management needs to ensure that HR activities should add value to the business. Today, managers are increasingly being asked to justify their decisions in financial terms. This development has proven to be especially difficult for HR managers as their activities are usually evaluated in behavioural /statistical terms rather than financial ones. In this paper the endeavour is primarily to examine the extent to which hotel companies can, and do measure the value of their human resources in financial terms. It also focuses on to promote an understanding and significant of HRA information for making vital Human Resource decisions in hotel companies in India.

Key Words: human resource accounting, hotel industry, human resource management

Today, tourism and hospitality is World's largest Industry and generates more than 12% of global GDP. It has emerged as a dominant economic giant on the global scene, accounting for more than 10% of the World trade and growing at the rate of 6.5% annually. The tremendous pace of development in this industry is further evident from the fact that it is a major employer, has created 255 million and 450 million jobs in 2000, and 2003, is likely to touch 538 million and 685 million by the years 2005 and 2006 respectively (2007). The labour-capital ratio per million rupees invested in hotel and tourism (74.2) is higher as compare to agriculture (49.7), railway (0.9) and manufacturing (15.7). Further, employment-output ratio is also higher in hotel and tourism (75), then textile (27), leather (51) and electricity (14), (2007).

Hotel industry in India, with its immense forex earnings; employment generation and enormous multifarious advantages, is currently one of the most competitive industries. It is also becoming increasingly global with many hotel companies operating at International scale like the Taj Group of Hotels, ITDC's Ashok Group of hotels, Welcomgroup of hotels; and the Oberoi Group of Hotels etc. The direct employment in the hotel sector has increased from 5.54 million in 1991-92 to 14.25 million in 2002-2003 and has touched 16.5 million by the year 2007.

Moreover, hospitality industry with its immense employment generation capability is very often called 'people intensive industry'. In this industry, human resources constitute a higher element of total operating cost. Obviously, the effective and extensive Human Resource Management (HRM) is critically significant to control the operating cost for long run survival. The Human Resource Policies and practices of every hotel company will have direct impact on procurement costs, quality human resources, delivery of quality products \ services and reduce employees turnover. Therefore, management needs to ensure that HR activities should add value to the business.

Today, managers are increasingly being asked to justify their decisions in financial terms. This development has proven to be especially difficult for HR managers as their activities are usually evaluated in behavioural/statistical terms rather than financial ones.

In this paper the endeavour is primarily to examine the extent to which hotel companies can, and do measure the value of their human resources in financial terms. It also focuses on to promote an understanding and significant of HRA information for making vital Human Resource decisions in hotel companies in India.

REVIEW OF LITERATURE

Managing human resources in an organization is one of the key elements of management (Mohinder, 2004). Whatever means are used to ensure the creation and delivery of services & goods in modern economic world, the role of individuals and groups as employees and the ability of management to effectively deploy such resources is vital in the interest of both employee and employer alike. In hotel industry management has recognised that it is the human element of service product that provides the key competitive advantage in the market place (Anastassova and Purcell, 1995). Therefore, human resources are managed with utmost care, accountability and rationality as other resources like, plant, building, machinery and finance etc. of the organisation. Unfortunately, employees turn over is very higher in lodging industry in comparison to other industries. It indicates as symptomatic of poor HRM systems and practices in this industry. The inputs of hotel industry are human beings and outputs are also human resources. Therefore, hotel manpower must gear itself to play more efficient and responsible role to meet the expectations of the International tourism. The standard of services in this industry is always measured with International pattern. Obviously, human resources are most important asset of this International Industry. (Now question is why people called as an 'Asset'?

Here, it becomes imperative to define human resources as 'an asset'. The exact definition of an asset is that it must possess future service potential, measurable in monetary terms and owned by the owner. There are some thinkers who refuse to treat human resources as an 'asset'. According to them HRs can not be disposed off or converted into cash. However, it is only a technical ground that the members of the staff are free to leave more or less at their will, the organization will replace them by others and thus the staff strength will more or less be maintained. Another opinion is that human resources do not give any assurance and do not have stored value like other assets e.g. building, machinery, and furniture etc.

However, this criterion of not treating human resources as *an asset* seems to carry no weight (Charles, 1974). In this world nothing is certain and no asset can give future assurance and stored valve. Even the debtors, bills receivable and other similar securities are not sure to be realized. Further, accountants argue that human resources are not owned by an organization and, hence they cannot be treated as an asset. But the actual fact is that, it is the investment in human resources and not the personnel themselves. Thus, there should not be any objection to treat human resources as an 'asset' and put the value in the position statement. Despite the some controversy outlined above, the Human Resource Accounting (HRA), literature does offer more useful and practical advice for determines the costs and values of this important 'Asset'. (Kiesoetal, 2003; Charaborty ,1976 and Arden ,1974)

A hotel company invests huge time and money in human asset and effective & efficient use of this asset is depends upon human resource information system (Mohinder and Anastasia, 2007). The technique which is used to identify, measure and reports about human resources is known as Human Resource Accounting'. Measuring the financial worth of human resources is not a new phenomenon, but it dates back in 1691's. It was William Petty, (1691) who has made the first attempt to value the people in financial terms. He was of the opinion that employee is the father of wealth and this must be taken into consideration while making an estimate of wealth. The various behavioural scientists in this field further made efforts to confine the term. However, the real work was started from 1960's. Rensis Likert (1961), an American sociologist, has originally popularised the concept 'Human Asset Accounting'. He has emphasized the need of HRA as a tool for Managerial decisions. Elias (1970) opined that the decisions based on Financial Accounting Information are quite different from those based on human resources accounting. Arden (1974) perceived that HRA data are more important for evaluating stock investment decision concerning organization with higher percentage of Managers, administrator, professionals and technical workers than the decision concerning with lower percentage of these workers. Charles (1974) the major function of HRM is the recruitment and retention of quality employees, which is largely based on the type of information provided to the decision-makers.

Many scholars have stated the need for more corporate financial transparency, and concerns that the omission of the value of human, structural and intellectual capital as organization assets results in an under-valuation of the knowledge based companies that drive the new economy (Grojer, 1997; Olsson, 1999, 2001a, b, 2003; and Kiesoetal, 2003). Further, it is argued that organizations acquire HR to generate future revenues, and therefore HR should be considered when valuing a company by capitalizing instead of expensing them in the current period (Flamholtz, 1995, 1999; Gröjer, 1997 and Mohinder, 1991). Thus, The crux of the argument is that human, intellectual, and structural capital should be treated in the same way as the things they are like; the things these advocates think they are most like are assets, and since assets are reported on the balance sheet, these also should be reported along with the physical assets (Cascio, 2000 and Schmidt et al., 1979).

There are many experts who have suggested methods \ models to determine the value of human resources in an organisation, such as Flamholtz ,1971, 1972 , 1975; Mores ,1973; Organ Pickin ,1974; Lawrence ,1975; Jaggi and Lev ,1974; N. Das Gupta ,1978; Jackson Floyat ,1978; S.K. Charaborty ,1976), and Fry Elaine hobbs ,1978) etc. But due to the practical utility of these methods and models; interest in exploring this vital field of accounting has declined in the early 1980's. Infect, organisations at that time have focused attention on labour as cost to be minimized. Obviously, method/models of HRA seemed to have limited significance for managerial decisions.

Business environment is changing rapidly in the 1990's. Moreover, in the wake of liberalisation and globalisation of Indian economy, the hotel industry is getting gradually internationalised and has stressed the need and importance to develop meaningful methods/techniques for evaluating the contribution of human resources in an organization. Practically, the following facts have increased the need of accurate, timely, reliable and understandable HR information for managerial decisions in hotel industry: -

- Development of Modern Organisation Theory
- Traditional Framework of Accounting has Changed
- Technology
- Development of Neo-human Relations Philosophy of People Management
- Development of modern management tools

RESEARCH METHODOLOGY

Numerous studies have suggested the implication of "Human Resource Accounting" in organizations. The conceptual framework presented in this article has drawn on literature from Human Resource Accounting, Human Resource Management, Management Theory, and Strategic Management. These fields of study were identified through a search of scholarly literature available primarily through electronic databases. The initial review of literature began with an examination of publications that discussed the concept of Human Resource Accounting and how this concept existed within organizations. The review process was then narrowed down to publications that referred specifically to the movement of managing human resources within organizations. The conclusion provides a discussion of implications for theory building and for practice in the hotel industry.

ACCOUNTING for HUMAN ASSET — Theoretical Perspective

During the last two decades number of approaches has been developed to measure the cost and value of human resources in the organisation. The brief discussion of these is as:

Historical Cost: Human resources are valued at the unexpired portion of the costs of recruiting, selecting, hiring, training, familiarization and development of employees of an organization. Moreover, the unexpired value is shown as an investment in human asset. This method is very simple and meets the tests of traditional Accounting Principle 'Matching costs with revenue'. However, the management need human resource information about the present and the future like what is the value/cost of human resource today and how are these costs/values changing. This approach does not fulfil these requirements.

Replacement Cost: This method suggested and developed by Rensis Likert and G. Flamholtz. It estimates the cost of replacing the existing employees under existing organizational conditions. Human resources of an organization are to be valued on the assumption that a new similar organization is to be created from scratch and then estimates the cost required for this purpose. It takes into consideration the fluctuations in jobs and general rise in price level in the market. Obviously, this method incorporates the current value of company's HRs. However, it is very difficult to find identical replacement cost of the existing personnel in actual practice. Further, the determinations of a value/cost will be affected by the subjective considerations to a marked extend and different managers/accountants may arrive at quite different estimates.

Opportunity Cost: According to Hekimian and Jones the human resource values/costs are measured through a competitive bidding process within the company known as opportunity cost. It is the value of an asset when there is an alternative use of it. The investment centre managers will bid for the scarce employees they need to recruit. The employees who are not considered scarce are not included in the value of HRs of the organization. This approach provides more optimal allocation of personnel and sets the quantitative base for decisions regarding *development of human asset.* However, this method results in lowering the morale and productivity of the human resources who were not covered in bidding process. Further, practically this approach provides inadequate information for managerial decisions.

Present Value of Future Earning Model: Under this model, the value of human resources is calculated as firstly; divide all personnel into homogeneous group according to their age and skill. Secondly, determine average Annual Earnings. Thirdly, Calculate total earning of each group up to retirement age, and fourthly use the cost of capital rate for capitalizing the present value of the future earnings of the employees. In other words, the model involves valuation of 'Human Assets' on the bases of the present value of the estimated future earnings of the employees discounted at the cost of capital rate. This basis of valuation of HRs is quite complicated and overstates an employee's expected service life and his future earning. Moreover, salaries paid to personnel may not really represent the human resource(s) a real worth to the organization.

Stochastic Reward Valuation Model: This model is based on estimated expected future services and is mainly concerned with the problem, how to determine the value of an individual to an organization. An individual value to an organization is his expected realizable value. It is estimated on the basis of the present worth of the set of future services he is expected to provide during the period he is likely to stay with the organization. Theoretically, this is the best model as it estimates, 'the present value of expected future services and considers human resources as 'an asset'. However, it is quite complicated to obtain realizable value, as it requires detailed manpower planning which is not feasible.

Aggregate Payment Model: This model considers the human resources of an organization as a group rather than individual and determines the values/ costs on this basis. However, Managerial and Non-Managerial personnel can be valuated separately. The value of HRs is determined by multiplying the average salary of the group with the average tenure of the employees of that group and discounted at the expected average (after tax) return on capital employed over the average tenure period to ascertain the present value of the estimated future payments. This method records the recruitment, hiring, selection, development and training costs separately and treated as deferred revenue expenditure. This method suggests that human resources should be shown under the head investments in the balance sheet.

Total Cost Approach: The total cost approach is different from all the method suggested by various scholars. Under this approach human resource value to an organisation is equal to total cost incurred by the individual, state and the organisation in bringing individual up to that position or making him fit for appropriate employment in the organisation. In other words, cost of human asset is equal to cost of formal education and training plus cost of post employment. The determined value should be adjusted t the end of each year on the basis of individual age, seniority, status, experience, managerial abilities and performance etc. This model considers both human resources who are employed and unemployed. It seems to be sound theoretically. However, its practical utility is very difficult because it is based on certain factors, which may not be expressed in monetary terms precisely and objectively.

Besides the above discussed methods, many more models have also been sued like Net Benefit Model and Certainly Equivalent Net Benefit Model. These are based on net benefit received by the organisation from the services of its employees. In other words the value of human resources is equivalent to the present value of net benefits received by the organisation from the service of its employees. The major draw back of these models is the calculation of Net Benefit.

A critical analysis of the models/methods of human resource valuation has revealed that the HRA deals with number of variables that are very difficult to measure in financial terms. Discussion has also pointed out that these models based on unrealistic assumptions and no one method/model is both objective and meaningful. However, the present value of future earning model has found suitable on account of convenience and objectively. Further, it made clear that there is dire need to develop an appropriate model that should be based on both objective and subjective valuation of human asset and should provide a meaningful information, which assist management in decision-making.

Importance of HRA Information in Hotel Companies

In India, the hotel companies are require to prepare and present their financial statements (profit and loss account and balance sheet) as per the provision of the companies Act, 1956. The section 211 (2) and 211 (1) of the companies Act, 1956 require that the profit and loss account and balance sheet of every hotel company shall be prepared and presented with the requirements and Performa given in the part II of schedule VI and part I schedule VI respectively. Incidentally, the Act does not provide for disclosure of any significant information of human resources employed in a hotel company except that the companies have to give by way of a note to the profit and loss account, particulars of employees getting remuneration of Rs. 1, 44,000 per annum or more. However, there is nothing in the companies Act that prevents hotel companies from giving details about its 'Human Assets' by way of a supplementary information attached with its financial statements.

If we look at the annual reports of hotel companies in India like Indian Hotels Co. Ltd., East India Hotels Co. Ltd., Bharat Hotels Co.Ltd. and many more Etc. we find that chairman's report invariably contains the statements highlighting the significance of human resources. The Chairman of these companies makes their remarks that our employees are out most important assets and without their significant contribution; the present growth in the operation would not have been attained. These qualitative pronouncements reflect the role and importance of human asset in an organisation. But unfortunately the quantitative information to their value has not been shown in the financial statements till today. However, in practice, a few enterprises both public and private sector in India value their human resources in financial terms and incorporate this vital information in their annual reports.

The International Accounting Standard Committee (IASC) was established in 1973 to formulate Accounting Standards and to promote their worldwide acceptance and observance. The committee has so for published 30 International Accounting Standards. On the other hand the council of the Institute of Chartered Accountants of India (ICAI) has constituted the Accounting Standards Board (ASB) in 1977, to formulate accounting standards for the companies operating in India. The ICAI is the member of IASC and gives due consideration to International Accounting Standards. Although the IASC and ICAI have brought out (30 and 15) accounting Standards on most of the technical areas in accounting and have ensured their implementation by making them mandatory. Regretting, both the IASC and ICAI have not been able to bring any definite accounting standard for measuring 'Human Resource' cost/value to report in the financial statements. However, the existing accounting standards fully support the adoption of HRA for the purpose of meeting their own requirements in true sense (2005).

Accounting is in an age of rapid transition, its environment has undergone to vast changes during the last two decades and increasingly complex business environment requires increased investment by companies in human resources. This requirement is more intense in hotel companies as investment in recruitment, selection, hiring, training and development of employees is significant in these companies. According to Hopwood (1973), "Accounting system provide most important information which is intended to assist managers make decisions which are in agreement with their organisation goals." Hospitality management has been making decisions that directly/indirectly effect on organisation's human resources. HRA is a tool for evaluating change in the human assets and provides information to management for decision making regarding recruitment, hiring, promotion, training, transfer, retrenchment, planning of physical assets vis-à-vis human assets. It evaluates the expenditures incurred for imparting further education & training to employees in terms of the benefits drive by the company. Moreover, Human Resource Accounting helps in identifying the causes of high labour turnover, and locating the real cause of low return on investment, whether due to improper or under utilisation of physical assets or human assets or both. According to Likert ,1967), "Managers decisions may range from those which are directly attempt to enhance the value of the firms' human resources to those which systematically liquidate them in order to show greater short run profits. In any case these conditions are not recalled by the financial accounting reports." Robert Wright, 1977) has stated that, "the ratio of investment in human assets to total assets is an indicator of profitability of generating future profits. If human assets ratio is higher there will be the higher profitability and if lower then lower profitability". It implies that HRA is helpful for potential investors and other users in making long-term investment decisions.

DEVELOPING HRA SYSTEM for HOTEL INDUSTRY

We have described different methods \ models which could be used to determine value/cost of human resources in hotel companies. But the reasoning behind this is whether to introduce HRA system in hotel industry and which method(s) to apply-will require a considerable amount of professional judgment. In order to evaluate the practical implications of developing HRA system in a hotel company, let us discuss the process of designing and implementation of HRA system in hotel industry.

Fig 1: Process of Developing HRA System in Hotel Industry

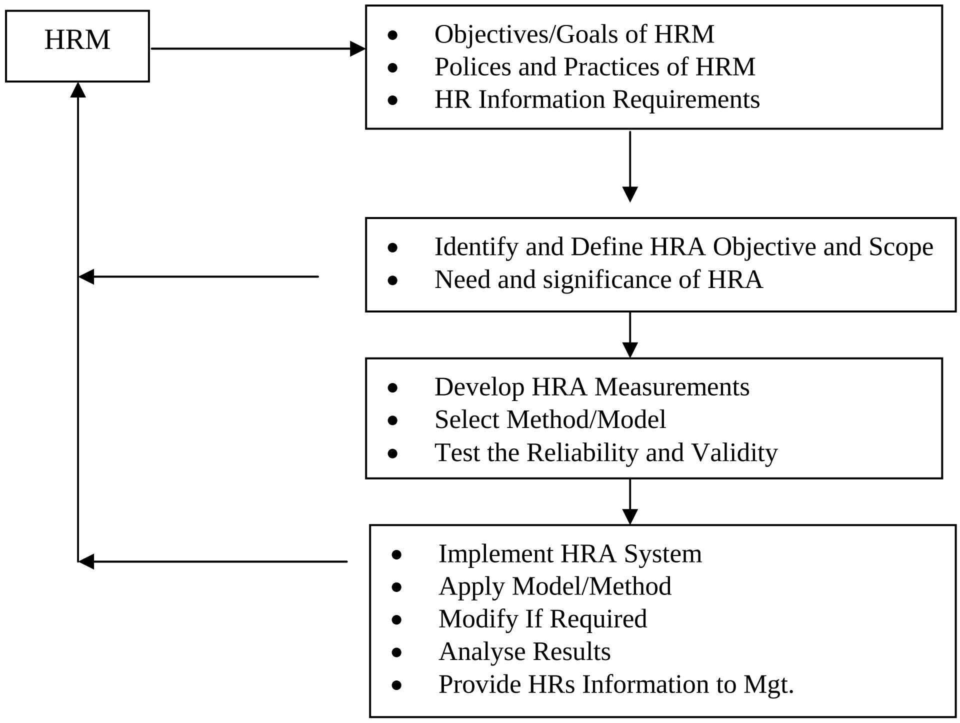

Fig. 1 shows design and development process of HRA system in hotel industry, it depicts four phases process which identifies the need and significance of HRA information for managerial decisions. Human resource management is defined as the process of developing people and lays claim to the achievement of organisation objectives. To assist HRM in fulfilling this major task, the accountants should provide appropriate human resource accounting information for decision making and inclusion in corporate report. The accountants should identify the objectives and scope of human resource accounting before developing the measurement. This analysis refers to the selection of the models/methods and than test the reliability and validity. The testing should be focused on a few factors/variables that appear to be critically important. Finally, the implementation of an HRA system should not be undertaken even it is acceptable, unless there are reasonable expectations that it will yield useful results over a period of time. Muscove (1983) "A well-developed HRA system can theoretically aid managers in becoming more effective and efficient in managing the human resources that are available to them". Moreover, one of the major functions of HRM is the recruitment and retention of quality employees and to increase its stock of human capital.
Development of an HRA system in Hotel industry is based on following factors/variables: -

- Size and Structure of Organisation;
- Organisation Climate;
- Top Management Support;
- Substantial Commitment of Time & Efforts; and
- Employees Co-operation

Despite number of factors affecting on HRA system in hotel industry, HRA will provide valuable information about human resources for inclusion in the corporate reports. Moreover, HRA will definitely be a power full tool in the hands of management to solve many employees' problems in the knowledge economy.

CONCLUSION and IMPLICATIONS

The hotel companies invest huge amount and time in human asset. Therefore, effective and extensive use of this important asset is obviously vital for long term survival of the hotel organisations. Unfortunately, financial accounting fails to incorporate the value/cost of 'human asset' in the annual reports, although the contribution and importance of human resources are often acknowledged in the Chairman's report. Incidentally, in the recent years this trend has changed and necessity of accounting for human resources has been increasingly realised. Today, HRA is recognised as a powerful managerial tool for proper management of human resources. It helps in developing such type of employment opportunities which can give higher rate of return on human capital, helps management to make more informal decisions regarding HRs, and suggests measures to determine the cost and value of human assets in the organisation. It established economic relationship between education and employment. It also helps in creating a feeling of social responsibility among individuals, which is the key to prosperity of any society or Nation. The present work has not included an attempt to construct an HRA model. The focus has been on illustrating the significance of human resource data for making effective managerial decisions in hotel companies rather than evaluating the relevant views and propositions. The explanatory comments have been designed to promote the understanding rather than to advocate the acceptance of HRA in hotel companies in India.

REFERENCES

Anastassova ,L.,and Purcell,K.(1995) Human resource management in the Bulgarian hotel industry: fromcommand to empowerment, *International Journal of Hospitality Management,Vol.14 No.2. pp. 171-85.*

Boudreau, J.W., Rynes, S.L. (1985) Role of recruitment in staffing utility analysis, *Journal of Applied Psychology*, Vol. 70 pp.354-66.

Brummet, R.L., Flamholtz, E., Pyle, W.C. (1968a) Accounting for human resources, *Michigan Business Review*, Vol. 20 No.2, pp.20-5.

Brummet, R.L., Flamholtz, E., Pyle, W.C. (1968b), Human resource measurement – a challenge for accountants, *The Accounting Review*, Vol. 43 pp.217-24.

Brummet, R.L., Flamholtz, E., Pyle, W.C. (1969b) Human resource myopia, *Monthly Labor Review*, Vol. 92 No.1, pp.29-30.

Brummet, R.L., Flamholtz, E., Pyle, W.C., Likert, R. (1975), *Human Resource Accounting: Development and Implementation in Industry*, Foundation on Human Behavior, Ann Arbor, MI.

Cascio, W.F. (2000) *Costing Human Resources: The Financial Impact of Behavior in Organizations*, 4th ed., South-Western College Publishing, Cincinnati, OH,

Chand, Mohinder (1991) Human Resource Accounting - A Case Study of LIC Shimla Division, An Unpublished M.Phil. Dissertation, H.P.U.

Edvinsson, L., Malone, M.S. (1997) *Intellectual Capital: Realizing Your Company's True Value by Finding its Hidden Brainpower*, HarperBusiness, New York, NY,

Ferguson And Bergar (1985) Employees As Assets: A Fresh Approach to HRA, The Council of HRA Quarterly 25.

Flamholtz, E.G. (1985) *Human Resource Accounting: Advances in Concepts, Methods and Applications*, Jossey-Bass, San Francisco, CA,

Flamholtz, E.G. (1999) *Human Resource Accounting – Advances in Concepts, Methods and Applications*, Kluwer Academic, Boston, MA,

Flamholtz, Eric G. (1985) Human Resource Accounting: Advances in Concepts, Methods and Applications, Jassey-Bass Publishers, London.

Gröjer, J.-E. (1997) Employee artifacts on the balance sheet: a model illustration and implications, *Journal of Human Resource Costing & Accounting*, Vol. 2 No.1, pp.27-53.

Hermanson, R.H. (1964) Accounting for human assets, Occasional Paper, No. 14, Graduate School of Business Administration, East Lansing, MI,

Hopwood, Anthony G., (1972) An Empirical Study of The Role of Accounting Data In Performance Evaluation, Journal of Accounting Research 10.

Hopwood, Anthony G., (1973) Problems with Using Accounting Information in Performance Evaluation, Management International Review, No. 2-3.

Hopwood, Anthony G., (1974) Human Asset Accounting, Administrative Staff College Henely, London.

Likert, Rensis, (1967) The Human Organisation: Its Management and Value, Mcraw Hill Book Company New York.

Maher, A., (1993) Accounting for Human Resources in UK Hotels: Some Initial Findings, Paper Present at the Council for Hospitality Management Education Research Conference, M.M. University.

Mayo, A. (2004) "Measuring human capital", *Worldwide Link*, Vol. 14 No.2, pp.3.

Mohinder C. (2004) Human resource strategies and global competitiveness: a study of Indian small and medium sized tourism enterprises, paper presented at the *International Conference on Creating Global Competitive Advantage*, Laxpara Foundation India.

Mohinder C. and Anastasia A.K., (2007) The impact of HRM practices on organisational performance in the Indian hotel industry, *Employee Relations*, vol.29 No.6, pp.576-94.

Muscove, S.A. (1983), A Further Investigation into Human Resource Accounting, Journal of Accountancy.

Scarpello, V., Theeke, H.A. (1989) "Human resource accounting: a measured critique", *Journal of Accounting Literature*, Vol. 8 pp.265-80.

The Hindu, 13th May 1998.

The Indian Institute of Chartered Accountant (2005) Report.

The World Travel and Tourism (2005 & 2007)

Travel and Tourism's Economic Perspective, A Special Report, Belgium.

Times of India 26th July 1995.

Tourist Statistics (2007 Deptt. of Tourism, Ministry of Tourism Govt. of India New Delhi.