

Human Resource Accounting – A Conceptual Analysis

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ABSTRACT

Management of any concern continuously strives hard for obtaining maximum efficiency. In order to measure the effectiveness of any firm the normal method is to examine financial statements. These statements include balance sheets in which physical assets such as cash accounts receivables, inventory and plant are recorded. These statements normally do not mention the productive capacity of the workers or goodwill of the company.

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INTRODUCTION

Human Resource Accounting (HRA) offers constructive information to both internal and external users of accounting information. It helps internal users (like management) in making decision on employment and utilization of human resources and also in deciding transfers, promotion, training and retrenchment of human resources. It provides a source for the development of physical assets - human resources, as well in assessing the expenditure incurred for imparting further education, training and development in employees in terms of the benefits derived by the firm, among others. For external users (such as potential investors), HRA provides useful information for making investment decisions. Many studies have been carried out on the behavioral and organizational aspects of accounting, but a lot of criticisms have developed in the area of HRA (Topomy, 2009). Organizations usually state that their labour force is their most important asset, but at the same time, they fail to recognize it in planning, decision-making and in published annual reports. Moreover, the probable usefulness of HRA information would appear to be even greater for the external decision-makers than for the company's management (Bratton and Gold, 2003).

Human Resource Accounting is the measurement of the cost and value of people to the organization. It involves measuring costs incurred by the organizations to recruit, select, hire, train and develop employees and judge their economic value to the organization.

Accounting is a man-made art and its principles and procedures have been evolved over a long period to aid business in reporting for the management and public. Of the four factors of production, viz., man, money, material and land, the last three of them are amenable to conventional accounting, but the first one, i.e., the human resource has not been subject to such accounting. Over the last two decades the idea of accounting for human resources is gaining active consideration.

Much of the work on accounting for human resources focused primarily on development or validation of HRA concepts. The traditional practice of treating all expenditure on human capital formation as an immediate charge against income is not consistent with the treatment accorded to comparable outlays in physical capital. The American Accounting Association strongly criticized the practice of assigning a Zero value to an asset and stated that 'Costs should be capitalized when they are incurred in order to yield future benefits and when such benefits can be measured.'

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HRA is the art of valuing, recording and presenting systematically the work of human resources in the books of accounts of an organisation. Thus, it is primarily an information system, which informs the management about the changes that are taking place in the human resource of an organisation.

DEFINITION OF HUMAN RESOURCE ACCOUNTING

Mr. Woodruff Jr. Vice President of R. G. Batty Corporation defines it as follows:

"Human Resource Accounting is an attempt to identify and report investments made in human resources of an organization that are presently not accounted for in conventional accounting practice. Basically it is an information system that tells the management what changes over time are occurring to the human resources of the business."

M.N. Baker defines Human Resource Accounting as follows:

"Human resource accounting is the term applied by the accountancy profession to quantify the cost and value of employees to their employing organization"

HISTORICAL DEVELOPMENT OF HRA

Stage 1 1960–1966 The origin of Human Resources Accounting with theories, representing inference of the basic concepts (primary) of human resource accounting.

Stage 2 1967–1970 The first basic academic formulation of some measuring models

Stage 3 1971–1977 Rapid increase in interest levels in Human Resources Accounting

Stage 4 1978–1980 Static academic interest level and emphasis on fixed assets in organizations led to the reduction of interest in HRA at the level of organizations and universities

Stage 5 1981–1990 Resurgence of international interests in theories and jobs in Human Resources Accounting.

Stage 6 1990–now Development of concepts, models, approaches, disclosure, accounting standards and treatment, generating soft information.

Source: Flamholtz (1999) and further developed by the author.

METHODOLOGY OF THE STUDY

Human resource accounting categorizes measures and provides information on the amount of expenditure incurred and the capital employed to recruit, train and make acquainted and develop the human resources. The objective of this paper is:

1. To study the concept of Human Resources accounting.
2. To study the issues and challenges.

The study is a descriptive and conceptual research wherein the author has used only the secondary data and the books and the publications to generate ideas on how the Human resource Accounting is taken up by the HR department of various industries. The paper is to provide handful of insight on basics of Human Resource Accounting and help the users to understand it fundamentally.

WHY HUMAN RESOURCE ACCOUNTING

The Industries and corporate in India rarely follow this kind of accounting and there are very few companies which follow or initiated the inclusion of Human Resource Accounting.

1. Under conventional accounting, no information is made available about the human resources employed in an organization, and without people the financial and physical resources cannot be operationally effective.
2. The expenses related to the human organization are charged to current revenue instead of being treated as investments, to be amortized over a period of time, with the result that magnitude of net income is significantly distorted. This makes the assessment of firm and inter-firm comparison difficult.

3. The productivity and profitability of a firm largely depends on the contribution of human assets. Two firms having identical physical assets and operating in the same market may have different returns due to differences in human assets. If the value of human assets is ignored, the total valuation of the firm becomes difficult.
4. If the value of human resources is not duly reported in profit and loss account and balance sheet, the important act of management on human assets cannot be perceived.
5. Expenses on recruitment, training, etc. are treated as expenses and written off against revenue under conventional accounting. All expenses on human resources are to be treated as investments, since the benefits are accrued over a period of time.

Benefits and gain Industries make by accounting the physical assets and including such items in the financial statements:

1. The system of HRA discloses the value of human resources, which helps in proper interpretation of return on capital employed.
2. Managerial decision-making can be improved with the help of HRA.
3. The implementation of human resource accounting clearly identifies human resources as valuable assets, which helps in preventing misuse of human resources by the superiors as well as the management.
4. It helps in efficient utilization of human resources and understanding the evil effects of labour unrest on the quality of human resources.
5. This system can increase productivity because the human talent, devotion, and skills are considered valuable assets, which can boost the morale of the employees.
6. It can assist the management for implementing best methods of wages and salary administration.

INDIAN SCENARIO

As far as the statutory requirements go, the Companies Act, 1956 does not demand furnishing of HRA related information in the financial statements of the companies. The Institute of Chartered Accountants of India too, has not been able to bring any definitive standard or measurement in the reporting of human resources costs. There are a few organizations, however, that do recognize the value of their human resources, and furnish the related information in their annual reports. In India, some of these companies are : Infosys, Bharat Heavy Electricals Ltd (BHEL); the Steel Authority of India Ltd. (SAIL), the Minerals and Metals Trading Corporation of India Ltd. (MMTC), the Southern Petrochemicals Industries Corporation of India (SPIC), the Associated Cement Companies Ltd, Madras Refineries Ltd. , the Hindustan Zinc Ltd. , Engineers India Ltd, the Oil and Natural Gas Commission, Oil India Ltd., the Cement Corporation of India Ltd. etc.

CONCLUSION

Human Resource Accounting is yet to gain momentum in India due to certain difficulties. The valuation methods have certain disadvantages as well as advantages; therefore, there is always a bone of contention among the firms that which

method is an ideal one. There are no standardized procedures developed so far. So, firms are providing only as additional information. Under conventional accounting, certain standards are accepted commonly, which is not possible under this method. All the methods of accounting for human assets are based on certain assumptions, which can go wrong at any time. For example, it is assumed that all workers continue to work with the same organization till retirement, which is far from possible. It is believed that human resources do not suffer depreciation, and in fact they always appreciate, which can also prove otherwise in certain firms. The lifespan of human resources cannot be estimated. So, the valuation seems to be unrealistic.

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