

## **Human resource accounting “our main asset is our people’**

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### **Abstract:**

In this changing and challenging times, when technology is becoming a great leveler, We are sure that it is people and people alone, who can make the difference and catapult the organisation to greater and yet unconquered heights- We believe that the talent innovation, creativity, business acumen and capabilities of people are the single most dependable source of competitive strength to the organisation. Human resources play the most important part in the development of an enterprise. Human resource accounting (HRA) is a measure the value of employees, which helps management, take the vital decisions related to human resources in order to increase productivity. It requires the measurement of the performances of an organisation and the optimum use of the resources under its direct and indirect control.

**Purpose** — The purpose of this paper is to establish that the competitive position of a firm depends on its specific assets. The most specific asset that an enterprise has is its personnel. It takes advantage to their interdependent knowledge and this is the reason why some firms are more productive than others. With the same technology, a solid human resource team makes all the difference. The value of a person as a resource depends on how he is employed; therefore, management style also influences the human resource value.

This paper examines the various models of human resources accounting (HRA) for valuing human in an organization. It gives an overview of the HRA models adopted by the public sector and software companies in India. The paper mentions the advantages and the hurdles in adopting HRA models in India. Finally, the paper also examines how ethos and culture effect the quality of work and how they can be accounted in books of accounts.

**Challenge** :— Fill past decade, the “value” of an enterprise was measured as an asset within traditional balance sheets, e.g. buildings, production plant. etc. This was viewed as a sufficient reflection of the enterprise’s assets. However, with the emergence of the knowledge economy, this traditional valuation has been called into question due to the recognition that human capital is an increasingly important part of an enterprise’s total value. But the question arises that how the value of human capital can be assessed. Providing adequate and valid information on human resources in statistical terms and within traditional balance sheet has proved extremely difficult.

**Design/methodology/approach**—Through this paper an attempt has been made to account for Human Resource maintaining the key parameters: correctness, transparency, prudence, and timeliness. A detailed revision is made of the main costs related to human resources: training and selection costs and exit costs. This analysis is made from the points of view of external and internal (or managerial) accounting on the basis of historical costs and opportunity costs.

**Findings**— Despite the fact that human resource functions are being diverted to low cost service providers the work ethos plays an important role in ensuring quality and productivity. Unfortunately the work ethos or culture of service providers is yet to be incorporated in the accounting system. It is a challenge to incorporate the ethos value but it would be achieved by measuring the final result from different service providers.

**Practical implications** — The methodology proposed in this paper can represent a potential guideline for a wide range of researches concerning the quality of accounting information.

## **INTRODUCTION**

### **DEFINITION OF HUMAN RESOURCE ACCOUNTING :-**

- Accounting for human resources deals with the measurement of costs which are associated with recruitment, selection, training, placement and developing the employees in the organisation. This also involves measuring the present economic value of human.
- Human Resource Accounting (HRA) is basically an information system that conveys to the management the changes that are occurring over time to the human resources of the business. HRA also involves accounting for investment in personnel and their replacement costs, and also the economic value of people in an organisation.

### **DEFINITION**

- Human resource accounting (HRA) is the process of identifying, measuring and communicating information about human resources in order to facilitate effective management within an organisation. It is an extension of the accounting principles of matching costs and revenues and of organising data to communicate relevant information in financial terms.
- HRA is to record report and analyse human resource related figures through the accounting system.

### **NEED FOR HUMAN RESOURCE ACCOUNTING**

- In this changing and challenging times, when technology is becoming a great leveler. We are sure that it is people and people alone, who can make the difference and catapult the organisation to never and yet unconquered heights. We believe that the talent innovation, creativity, business acumen and capabilities of people are the single most dependable source of competitive strength to the organisation. Human resources play the most important part in the development of an enterprise. Human resource accounting (HRA) helps to measure the value of employees which helps management, take the vital decisions related to human

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resources in order to increase production. It requires the measurement of the performances of an organisation and the optimum use of the resources under its direct and indirect control.

- Human capital is the most important asset in service oriented organisations.
- In the present scenario importance shifts from financial capital to intellectual capital.
- Present accounting system ignores the importance of human resources value. Most human capital related costs are treated as expenses, instead of assets.
- Financial ratios based on financial statements and provided very little information on human capital.

### **ADVANTAGES OF HUMAN RESOURCE ACCOUNTING**

- It helps in giving valuable information to the management for effective planning and managing human resources.
- It helps in measurement of standard cost of recruiting, selecting, hiring and training people and organisation can select a person with highest expected realisable value
- Information generated by HRA systems can be put to use for taking a variety of managerial decisions like recruitment planning, turnover analysis, personnel advancement analysis and capital budgeting, which can help companies avoid a lot of trouble in the future.
- HRA provides necessary data to devise suitable promotion policy and job satisfaction to the people.
- Appropriate accounting of the human resources would allow an estimate of the productive capability of the organization.
- Worldwide, knowledge has become the key determinant for economic and business success, but Indian companies focus on Return on Investment’ (RoI), with very few concrete steps being taken to track Return on Knowledge”.

### **Problems in Human Resource Accounting**

- There is no well-set standard accounting practice for measuring the value of human resources.
- If the valuation is not done correctly the HRA may lead to the dehumanization in the organisation.
- The valuation of human resource is based on the assumption that employees may remain with the organisation for certain specified period.

### **Valuation of Human Assets**

- The current accounting system is not able to provide the actual value of employee capabilities and knowledge. This indirectly affects future investments of a company, as each year the cost on human resource development and recruitment increases.

- The major methods of valuation of human assets are

1. Historical Cost
2. Replacement Cost
3. Standard Cost
4. Present value of the future earnings.
5. Expected realisable value

### **Historical Cost**

- This method measures the organisation's investment in employees using the five parameters: recruiting, acquisition, formal training and familiarisation, informal training experience and development.
- This cost can be further divided into two types — Acquisition cost and learning cost.
- Acquisition cost is the expense incurred on recruiting and acquisition, whereas.
- Learning cost is the expense incurred on training and development.

### **Limitations**

- This method measures only the cost to the organisation but ignores completely any measure of the value of the employee to the organisation. Example: An experienced employee may not require much training and therefore his value may appear to be low though his real value is might be very high.
- Since the assets cannot be sold there is no independent check on valuation.

### **Replacement Cost**

- This approach measures the cost of replacing an employee. This cost includes recruitment, selection, compensation and training cost. This cost also includes the opportunity cost from lost revenue during the period of training. The data derived from this method could be useful in deciding whether to dismiss or replace the staff.

### **Limitations**

- Substitutions of replacement cost method does little more than update the valuation at the expense of importing considerably more subjectivity into the measure. This method may also lead to an upwardly biased estimate because an inefficient firm may incur greater cost to replace an employee.

### **Standard Cost**

- It is the cost that ought to be incurred to attain some specified end under predefined conditions. Thus standard cost concept is hypothetical a target for what costs ought to be.

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- According to this method, employees of an organization are categorized into different groups based on their hierarchal position. Standard cost is fixed for each category of employees and their value is calculated. This method is simple but does not take into account difference in employees put in the same group.

### **Limitation**

- This method does not consider the efficiency of individual employee, it treats all the employee in the hierarchal position to be equal.

### **Present Value of Future Earnings**

- In this method, the future earning of various groups of employees are estimated upto the age of their retirement and the discounted at a predetermined rate to obtain the present value of such earning. However this method does not give current value of human assets as it does not measure their contribution to achieving the objectives of the firm. This method is based on the assumption that there is no direct relationship between cost incurred on an individual and his value for the organization.

### **Limitations**

- The measure assigns more weight to averages than to the value of any specific group or individual.
- The measure is an objective one because it uses widely based statistics such as census income return and mortality tables.

### **Expected Reusable Value**

- An individual's value to an organization is the sense of the expected reliable value and it can be measured by applying personnel evaluation methods like ranking. Individuals may be evaluated by their superiors, peers, subordinates or an independent expert according to their expected reusable value to the organization. When people are ranked by the evaluator it would provide an ordinal measure of people according to the evaluators subjective assessment of the expected realizable utility. A true measure of their economic value should be possible in terms of their net contribution to the organization that is their gross value, less the compensation and other costs associated with their utilization.
- The major individual determinants to conditional value are the skills and motivation of the individual and the major organizational determinants are the individual's role and the nature of organizational rewards. However to determine an individual's expected realizable value, it is also necessary to take into account the probability of the individual maintaining his membership of the organization for a specified period of time. For this purpose actuarial probabilities can be derived from the firm's past history, and subjective probabilities can be derived from managerial judgement.

### **Work Culture, Ethos and Loyalty**

- It is truly said that a person learns more and better through experience than through education and training but the experience and loyalty does not form the part of Human Resource Accounting as the amount is not spent on training.
- In past two decades technology has changed substantially, as a result it has become possible to separate the human resource functions such as pay roll maintenance, accounting, invoicing, etc. from other basic functions of the organisation. Despite the human resource function being diverted to low cost service providers. Despite the human resource function being diverted to low cost service providers the work ethos plays an important role in ensuring quality and productivity. Unfortunately the work ethos of culture of service providers is yet to be measured and incorporated in the accounting system.
- Although not accounted in books of accounts, but the culture and ethos play a very important role in determining the price of the product. For example a product made in Japan demands high price in comparison to the same product made in China. This is because the work image of Japan is that of high quality and that of China is of cheap and low quality. It is a challenge to incorporate the ethos value but it could be achieved by measuring the final result from different service providers.
- Presently the outsourcing of jobs is done from the developed countries like USA, England and to the underdeveloped and developing countries. [The selection of the service provider does not only depend on the cost but also on the quality and work culture. The same work could possibly be got done at a cheaper price from Bangladesh or Pakistan in comparison to India but the work is being done in India and this is due to quality of work.
- The firms are getting these jobs because of the staff (quality staff) they have and this should definitely get place in Balance Sheet through Human Resource Accounting. The experienced staff which is loyal to the organization and hence attached to the organization for years is not given place in human resource accounting as per historical cost method because amount is not spent on his training. This is no way acceptable as such staff should be given the maximum value in the human Resource accounting.

### **Accounting of Loyalty of Staff, Culture and Ethos**

- Accounting of Loyal staff should be on the basis of the cost that is saved by their presence in the organisation. Although amount is not being spent on their training but definitely cost is being saved by not spending on their training etc. The staff which is attached with the organisation for years is probably the biggest asset for the organisation. The organization can rely on them and their job experience can be of great help to the organization. The experienced staff's value can be shown as the cost saved by retaining them.
- Similarly Culture and Ethos of the staff is also an asset to the organization. A Japanese employee is paid more salary than an Indian employee only because their goodwill of culture and ethos backs them. The value of motivated and sincere staff would definitely be much more than the cost spent on motivating them to be sincere. The value of staff with such culture can

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he calculated on the basis of the final output given by them and the quality of the work done by them.

**Conclusion :** Loyalty of staff, Culture and Ethos of stall should be covered under Human Resource Accounting and should get place in the Balance Sheet.