

A Study of Human Resource Accounting Methods and Practices in India

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Abstract

This paper portrays the appreciation and need of human resource accounting importance and development with different approaches of the organisation in India .The human resource accounting helps individual employees in improving their performance and bargaining power. It makes each of them conscious of the contribution that he is making towards the betterment of the firm vis-a-vis the expenditure incurred by the firm on him. It is widely accepted fact that success of any organisation of business or otherwise, to a great extent, depends upon the quality, calibre and character of the people working in it. Objectives of the study of Human Resource Accounting helps to know the present empirical evidence, value of human resources assets can assist organizations in efficient and effective manner.

Key words: Human resource Management, human resource value, cost, price.

Introduction:

It is widely accepted fact that success of any organisation or otherwise, to a great extent, depends upon the quality, calibre and character of the people working in it. Human resource Accounting is the process of identifying and measuring data about human resource and communicating this information to interested parties.(or) Human resource Accounting is the process of identifying and reporting investments made in the human resources of an organization that are presently unaccounted for in the convention accounting practices. An organisation having vast physical resources, with latest technology, may find itself in the midst of several financial crisis. In case it does not have right people to manage and conduct its affair. The concept of considering human beings as an asset is an old phenomenon that effort was made to assign any monetary value to such individual in the balance sheet of the nation or organisation. According to the American Accounting Society, Human resource accounting is the process of identifying and measuring data about human resources and communicating this information to interested parties.

Origin

The first attempt to value the human beings in monetary terms was made by Sir William petty as early as 1691.petty was of the opinion that labour was “the father of wealth” and it must be included in any estimate of national wealth. Further efforts were made by William Far in 1853, Earnest Engle in 1883. However, the real work on the subject started from 1960, when behavioural scientists vehemently criticised, the conventional accounting practice of not valuing the human resource along with other material resources. As a result, accountant s and economists all over the world become conscious of the fact the appropriate methodology and procedure have to be developed for finding cost and value of the people to the organisation. Over the period of three decades, a number of experts have worked on it and produced certain models for evaluating human resources.

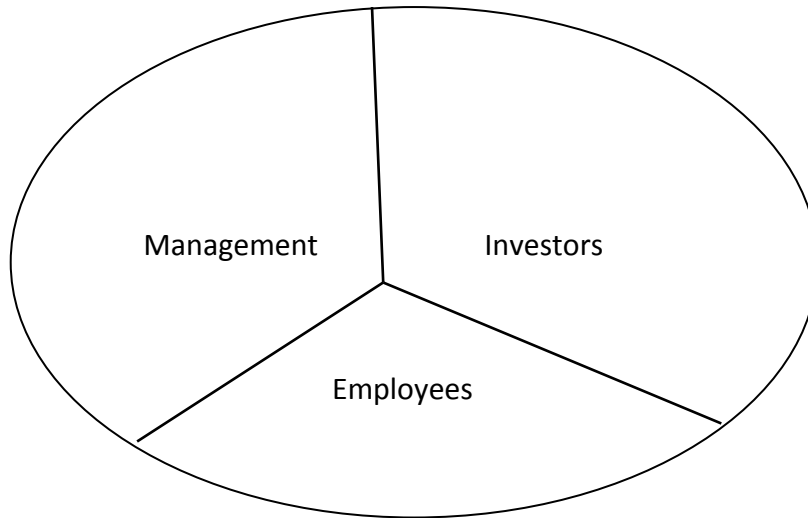
Objectives

The Human resource accounting process was established to fulfil a number of objectives within the organisation. These include:

1. To furnish cost value information for making proper and effective management decisions about acquiring, allocating, developing, and maintaining human resources in order to achieve cost effective organizational objectives.
2. To monitor effectively the use of human resources by the management.
3. To have an analysis of the human asset, i.e. whether such assets are conserved, depleted or appreciated.

4. To aid in the development of management principles and proper decision making for the future, by classifying financial consequences of various practices.

Importance:



Human resource accounting provides useful information to management, financial analysts (investors) and employees, as shown below

Management: Helps the management in decision making process relating to various matters.

- (a). Employment, locating and utilisation of human resources.
- (b). Transfers, promotion , training and retrenchment of human resource.
- (c)Planning of physical assets via-a-vis human resources.
- (d) Evaluating the expenditure incurred for imparting further education and training to employees in terms of benefits derived from firms.
- (e) Identifying the causes of high labour turnover at various levels and take preventive measures to contain it.
- (f)Locating the real cause of .low return on investment, that whether due to improper or under – utilisation of physical assets or human resources or both

Investors : (a) financial analysts is interested in understanding and assessing the internal strength of the firm which means physical assets owned and possessed depending upon the human resources by the firm.

(b) The vigilant, dynamic and responsible management can steer the company well through most adverse and unfavourable circumstances

Employees

Human resources accounting helps employees their capability and capacity of the individuality. They know how their value the assets of human resouces are treated in the organistion and also in need of improvement on both side of decision making.

The valuation of human resources depends on three important aspects such as (i) valuation of human resources.(ii) recording the valuation in the books of accounts and (iii) disclosure of the information in the financial statements of the business.

Valuation of human resources

In order to quantify for talent, skills and knowledge of employees or work forces in the organisational, by how for efficient calculated under various methods. The importance approaches for valuation of human resources are given below:

1. Historical Cost Approach:

This approach was first developed by William C.Pyle (and assisted by R.Lee Brummet & Eric G.Flamholtz) and R.G.Berry corporation, a leisure footwear manufacture based on Columbus, Ohio (USA) in 1967. Actual cost incurred on recruiting, hiring, training and developing the human resource of the organisation are capitalised and amortised over the expected useful life of the human resources.

Merits

- (i) This method is simple to understand and easy to work out.
- (ii) This method follows the traditional accounting concept of matching cost with revenue.
- (iii) It provides a basis for valuing a firm's returns on its investment on human resources.

Demerits:

- (i) It does not consider the aggregate value of their potential services.
- (ii) It is difficult to estimate the period over which the human resource will provide service to the organisation.
- (iii) It thus creates problems in determining the amount to be amortised over the year.

2. Replacement cost approach:

It was developed by Rensis Likert and Eric G.Flamholtz. This approach values the human resources at their present replacement cost on the basis of the assumption what would cost the firm, if the existing human resources are required to be replaced with others of equivalent talents and experience. It allows for changes in the cost for acquiring, training and developing the employees in place of taking their historical cost for capitalisation.

Merits:

This approach incorporates the current value of the firm's human resources and thus, the financial statements prepared are more realistic.

It is almost impossible to ascertain correct replacement cost of existing human resources since there can be no complete replacement for them.

Demerits:

- (i) The method is at variance with conventional accounting practice of valuing assets at historical costs.
- (ii) It is almost impossible to ascertain correct replacement cost of existing human resources there can be no complete replacement for them.

3. Opportunity cost approach:

It has been suggested by Hekimian and Jones for a company with several divisional heads bidding for the services of various people they need among themselves and then include the bid price in the investment cost. Opportunity cost is the value of an asset when there is an alternative use of it. If there is no scare of employees, there will be no opportunity cost. As such, only scarce people should comprise the value of human resources.

Merits:

- (i). This method can work for some of the people at shop floor and middle order management.
- (ii). This approach believes that a bidding process such as this is a promising approach towards more optimal allocation of personnel and a quantitative base for planning, evaluating and developing human assets of the firm.

Demerits:

- (i) It has specifically excluded from its preview the employees who are not scarce or are not being bid by the other departments

(ii).It result in lowering the morale and productivity of the employees who are not covered by the competitive process.

(iii)The total valuation of human resources on te competitive bid price may be misleading and inaccurate, due to the reason that a person may be an expert and valuable person for the department in which he is working and thus command a hig value but may have a lower price in the bid by the other department.

4. Standard Cost Approach

This approach envisages establishing of a standard cost per grade of updated every year. Replacement costs can be used to develop standard costs of recruitment, training and developing individuals. But under this approach determination of the standard cost for each grade of employee is at constant process. Standard cost is fixed for each category of employees and their value is calculated. This method is simple but does not take into account differences in employees put in the same group.

5. Present Value Approach

Under this approach, the value of human resources of an organization is determined according to their present value to te organization. The future earnings of various groups of employees are estimated up to the age of their retirement and are discounted at a predetermined rate to obtain the present value of such earnings.

Merits:

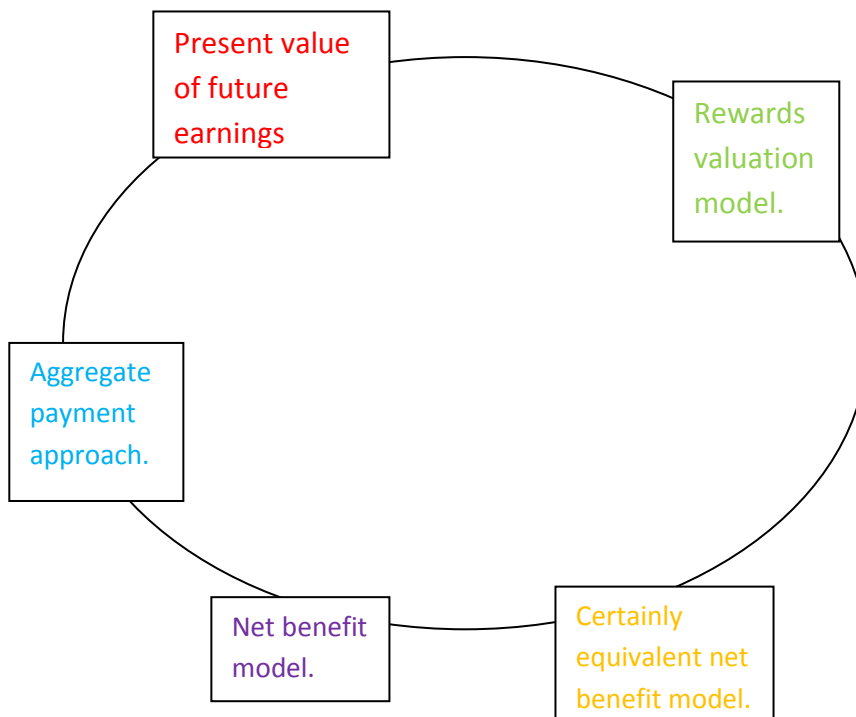
It is similar to the present value of future earnings used in the financial assets.

Demerits:

This method does not give correct value of human assets.

It does not measure their contributions to achieving organisational effectiveness.

A number of valuation models have been developed to determine the present value.



Present value of future earnings model

Developed by Lev and Schwartz in 1971 and is popular in India. This is also known as capitalisation of salary method. It is calculated by public sectors like SAIL and BHEL in which the future earnings of an employee or grades of employees are estimated up to the age of retirement and are discounted at a rate appropriate to the person or the group in order to obtain the present value.

Expected realizable value:

This method may provide information for record purpose but do not reflect the true value of human assets, as against these methods, Expected realizable value is based on the assumption. And this is true also. That there is no direct relationship between cost incurred on an individual and his value to organisation can be defined as the present worth of the set of future services that he is expected to provide during the period he remains in the organisation.

Flamholtz has given the variables affecting an individual's expected realisable value (IERV). While the later is a function of such variables as job satisfaction, commitment, motivation and other factors.

Economic value method: The economist's concepts of the value of an asset are equal to the present worth of its estimated future economic benefits. This approach has a strong theoretical appeal.

But this method involves the following steps:

- (a) Estimation of the future benefits, and
- (b) Ascertaining the present value of such benefits by using an appropriate interest (discount) rate;

Competitive Bidding Method:

This is also known as the opportunity cost method. Opportunity cost is defined as the measurable value of benefits that could be obtained by choosing an alternative course of action. In the case of human resource accounting, Opportunity costs are determined by a process of competitive bidding in which various divisions and departments bid for the services of various officers. The amount of bid is added to the capital employed of the successful bidder for determining the return on investment.

Example of human resource: The INFOSYS GIST- HCX model

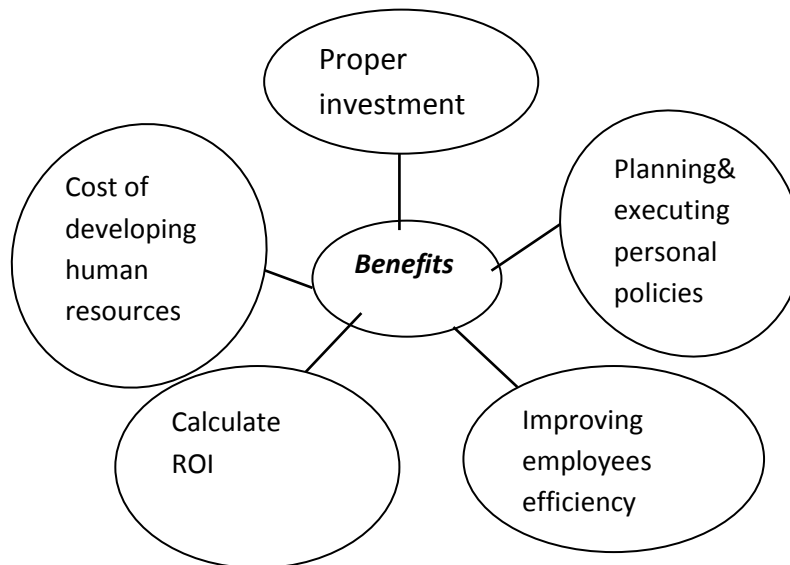
A fundamental dichotomy in accounting practices is between human and non-human capital is considered as assets and reported in the financial statement, whereas human capital is mostly ignored by accountants. The INFOSYS GIST- HCX model is based on a present value calculation of the increase in future earnings of employees during their employments at Infosys. The model discounts future earnings at an appropriate discount rate, and utilises the long-run inflation rate consistent with the Reserve Bank of India's target for inflation expectations.

In Rs.crore unless stated otherwise

Employees (no.)	2014	2013	Annual change
Software professionals	141788	123811	14.52%
support	8206	7009	17.08%
Total	149994	130820	14.66%
Value of human resources			
Software professionals	115900	89507	29.49%
support	9817	8640	13.62%
Total	125717	98147	28.09%
Value of human capital externality			
Software professionals	6182	4702	31.48%
support	649	563	15.28%
Total	6831	5265	29.17%
Total value of human resource capital and human capital externality	132548	103412	28.17%
Ratio			
Value of human capital per Employee	0.84%	0.75%	12.00%

Benefits of human resource Accounting

A good manager keeps the morale of his subordinates high so that they contribute the maximum in achieving the organisational objectives. The following are the main benefits of Human resource accounting,



1. Helps in proper interpretation of return on capital employed

The human resource accounting will disclose the value of human resources and will help in proper interpretation of return on capital employed.

2. Improves managerial Decision making:

The maintenance of detailed records relating to internal human resources (ie. Employees), will improve managerial decision making.

3. Serves social purpose:

It will serve social purpose by identification of human resources as a valuable asset which will keep prevention of misuse and under use due to thoughtless or rather reckless transfers, demotions, layoffs and day to day maltreatment by supervisors and other superior's in the administrative hierarchy.

4. Increase productivity:

It will have the way for increasing productivity of the human resources because, the fact that a monetary value is attached to human resources, and that human talent, devotion and skill are considered as valuable assets.

6. Invaluable contribution to humanity:

Human Resource Accounting will be an invaluable contribution of accounting to humanity and it will lead to improved human efficiency.

7. Essential where the human element is the prime factor.

8. Helps in investment decisions.

9. For successful operation of an organisation.

Limitations of Human resources accounting:

No doubt Human Resource Accounting can provide valuable information both for management and outsiders, yet its development and application in different industries and organisations has not been very encouraging.

1. There are no specific and clear out guidelines for finding cost and value of human resources of an organisation.

2. The life of human resources is uncertain and therefore, valuing them under uncertainty seems unrealistic.

3. There is a possibility that Human Resource Accounting may lead to dehumanising and manipulations in employees.

4. Human resources, unlike physical assets, are not capable of being owned, retained and utilised at the pleasure of the organisation.

5. There is a constant fear of opposition from the trade unions. Ie., Based on value of asset, employees seek reward compensation by placing the value on employees.

6. Tax laws do not recognise human beings as asset

Conclusion:

whatever development and technology came in the business, Human resources plays a vital role for any of the business held in the world .Depending upon the success of human resources, success of the organisation in which turn reflecting .Human resource accounting helps the human to know about the capacity and capability of the individual and for the organisation. Therefore any of the organisation success depends upon the success of the human resources.

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