



## AN OVERVIEW OF HUMAN RESOURCE ACCOUNTING IN INDIA

**Ruchi Jain, Ph. D.**

Assistant Professor, Department of Commerce, Hindu College, University of Delhi

Email : Ruchi26jain@gmail.com

### *Abstract*

*For a long period, the importance of human resource was not taken care of seriously by the top management of organizations. Therefore, at this juncture, it becomes imperative to pay due attention on the proper development of such an important resource of an organization. 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. Human resource accounting is the art of valuing, recording and presenting systematically the worth of human resources in the books of account of an organization.*

**Keywords :** *Human Resource Accounting, Human Resource, Human Resource Development*

### **Introduction**

The productivity of a company's investment is known from the rate of return it gives. So far, these rates of productiveness considered in respect of Physical assets only. To find out the productivity of investment on human beings in any organization human resource accounting emerged as a supporting tool. The Human Resource Accounting is a tool that generates and reports quantitative control information about the contribution of human resource in industrial productivity. There are two major reasons why Human Resources Accounting has been receiving so much attention in the recent years. First, there is genuine need for reliable and complete management of human resources. Secondly, a traditional framework of accounting is in the process to include a much broader set of measurement than was possible in the past. The people are the most important assets of an organization and yet the value of this asset does not appear in financial statements. Conventional accounting of human resources outlay consists of taking note of all expenses of Human capital formation which does not seem either to be correct or meeting the actual needs.

The American Accounting Society Committee on Human Resource Accounting defines it as follows: "Human Resource Accounting is the process of identifying and measuring data about human resources and communicating this information to interested parties."

Mr. Woodruff Jr. Vice President of R. G. Batty Corporation defines it as "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 "Human resource accounting is the term applied by the accountancy profession to quantify the cost and value of employees to their employing organization."

Thus, human resources accounting may be defined as, a process of accounting which identifies, quantifies and measures human resources for the use of management to cope up with the changes in its quantum and quality so that equilibrium could be achieved in between the required resources and the provided human resources.

### **Importance of Human Resource Accounting**

Human Resource Accounting provides useful information to the management, financial analysts and employees and its importance can be enumerated as:

1. It helps the management in the Employment, locating and utilization of human resources.
2. It helps in deciding the transfers, promotion, training and retrenchment of human resources.
3. It provides a basis for planning of physical assets vis-à-vis human resources.
4. It assists in evaluating the expenditure incurred for imparting further education and training in employees in terms of the benefits derived by the firm.
5. It helps to identify the causes of high labour turnover at various levels and taking preventive measures to contain it.
6. It helps in locating the real cause for low return on investment, like improper or under-utilization of physical assets or human resource or both.
7. It helps in understanding and assessing the inner strength of an organization and helps the management to steer the company well through most adverse and unfavourable circumstances.
8. It provides valuable information for persons interested in making long term investment in the firm.

9. It helps employees in improving their performance and bargaining power. It makes each of them to understand his contribution towards the betterment of the firm vis-à-vis the expenditure incurred by the firm on him.

### **Objectives of Human Resource Accounting**

The aim of HRA is to depict the potential of Human Resource (HR) in monetary terms, while casting the organization's financial statements. The concept can be examined from two dimensions: (i) the investment in HR; and (ii) the value of HR. The expenditure incurred for recruiting, staffing and training and developing the HR quality is the investment in HR. The fruits of such investments are increased productivity and profit to the organization. The yield that the investment generates is considered as the basis for HR value. The main objective of human resource accounting is to facilitate the management to get information on the cost and value of human resources. Human resources accounting brings to light the quantum of human resources and indicates the right control of conservation, depletion and appreciation of it in the right perspective. It provides data to the interested persons about the cost of human resources and correspondingly comparing it with the benefit obtained out of its utilization.

The objective of HRA is not merely the recognition of the value of all resources used by the organization, but also includes the management of human resource which will enhance the quantity and quality of goods and services. The basic objective of HRA is to facilitate the efficiency of human resource. It is basically adopted to treat human resources as assets, to generate human data about human resources, to assign value to human resources and to present human assets in the balance sheet.

The main objectives of a HR Accounting system are:

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.
5. In all, it facilitates valuation of human resources, recording the valuation in the books of account and disclosure of the information in the financial statement.
6. Further, it is to help the organization in decision making in the following areas:
  - a) Direct Recruitment Vs promotion.

- b) Transfer Vs. Retention.
- c) Retrenchment Vs. Retention
- d) Impact on budgetary controls of human relations and organizational behaviour.
- e) Decision on reallocation of plants, closing down existing units and developing overseas subsidiaries etc.

### **Literature Review**

Kenneth A. Klase (2007) “Accounting for Human Resource Development in Public Sector”. In this article, it evaluates the merits of utilizing human resource accounting concept to account for human resource development in public sector. It also describes the development of the economy theory of human capital and the increasing recognition of human resource as human assets of public organizations to be managed and accounted for in a similar manner to capital assets.

Steen and Welch (2011), By researching relevant human asset accounting and human resource literature, the study tried to investigate the idea of human capital and its valuation. Intangible costs and benefits are difficult to measure, according to the findings of this study. As a result, accurate human resource measurement remains a challenge.

Parsad C (2012) “Accounting for human capital is the balance sheet missing something?” The paper explains that traditional accounting practices do not classify human capital as an asset on the balance sheet. Based on the research it was analysed that majority opinion is not to include human asset as an asset in the balance sheet if did so it would inflate the value of assets of the company.

McKenna and Krishnan (2012), The purpose of the poll was to find out whether people thought human resources should be monitored and reported on the balance sheet. According to the survey, 87 percent of the nearly 500 accounting respondents are opposed to the value and reporting of human capital on the balance sheet. This result indicates that it is not universally recognized, and probable explanations for this include a lack of understanding about HRA and its advantages, as well as the difficulties associated with valuation and reporting. As a result, it's critical to figure out what's causing these outcomes.

### **Objectives & Research Methodology**

The purpose of this study is –

1. To familiarise with the Human Resource Accounting Practices in India.
2. To understand the significance of Human Resource Accounting.
3. To identify the issues and challenges related to Human Resources accounting.



The study is purely based on secondary data which is collected through various books, articles and research papers published in different national and international journals and various websites.

### **Overview Of Human Resource Accounting**

HR Professionals must perform a wide variety of functional roles. A functional role is a specific set of tasks and expected output for a particular job. The HR executive/manager has primary responsibility for all HR activities. This person must integrate the Human Resource Development (HRD) programs with the goals and strategies of the organization, and normally assumes a leadership role in the executive development program, if one exists. The outputs of this role include long-range plans and strategies, policies, and budget allocation schedules.

One of the important tasks of the HR executive is to promote the value of HRD as means of ensuring that organizational members have the competencies to meet current and future job demands. If senior managers do not understand the value of HRD, it will be difficult for the HRD executive to get their commitment to HRD efforts and to justify the expenditure of funds during tough times. Historically during financial difficulties, HRD programs and HRM has been a major target of cost-cutting efforts. Unless the HR executive establishes a clear relationship between HRD expenditures and organizational effectiveness (including profits), HRD programs will not receive the support they need. The role of the HR executive has become more important and visible as organization make the necessary transition to a global economy. The immediate challenge to HR executives is to redefine a new role for HRD during this period of unprecedented change.

According to Jack Bowsheer, former director of education for IBM, when HRD executives "delve deeply into reengineering, quality improvement, and strategic planning, they grasp the link between workforce learning and performance on the one hand, and company performance and profitability on the other."

The HRD executive is in an excellent position to establish credibility of HRD programs and processes as tools for managing in today's challenging business environment. As organization has adjusted to environmental challenges, the roles played by HR professionals have changed. Based on the ASTD (American Society for Training and Development) study results, Pat Mclagan states that contemporary professionals perform nine distinct roles, which are described below:

1. The HR strategic adviser consults strategic decision makers on HRD issues that directly affect the articulation of organization strategies and performance goals. Output includes HR strategic plans and strategic planning education and training programs.

2. The HR systems designer and developer assist HR management in the design and development of HR systems that affect organization performance. Outputs include HR program designs, intervention strategies, and implementation of HR Programs.
3. The organization change agent advises management in the design and implementation of change strategies used in transforming organizations. The outputs include more efficient work teams, quality management, intervention strategies, implementation, and change reports.
4. The organization design consultant advises management on work systems design and the efficient use of human resources. Outputs include intervention strategies, alternative work designs, and implementation.
5. The learning program specialist (or instructional designer) identifies needs of the learner, develops and designs appropriate learning programs, and prepares materials and other learning aids. Outputs include program objectives, lesson plans, and intervention strategies.
6. The instructor/facilitator presents materials and leads and facilitates structured learning experiences. Outputs include the selection of appropriate instructional methods and techniques and the actual HRD program itself.
7. The individual development and career counsellor assists individual employees in assessing their competencies and goals in order to develop a realistic career plan. Outputs include individual assessment sessions, workshop facilitation, and career guidance.
8. The performance consultant (or coach) advises line management on appropriate interventions designed to improve individual and group performance. Outputs include intervention strategies, coaching design, and implementation.
9. The researcher assesses HR practices and programs using appropriate statistical procedures to determine their overall effectiveness and communicates the results to the organization. Outputs include research designs, research findings, and recommendations and reports.

### **Challenges to organizations and HR Professionals**

Many challenges face organizations as a new century unfolds before us. Michael Hitt and his colleagues have identified increasing globalization and the technological revolution, in particular, the internet is a primary factor that make for a new competitive landscape, they suggest a number of actions that organizations can take to address the uncertainty and turbulence in the external environments. These actions include developing employee's skills, effectively using new technology, developing new organizational structures and building cultures that fosters learning and innovation. These obviously have a great deal to do with human resource development. The present five challenges currently facing the field of HRD include:

1. Changing workforce demographics.
2. Competing in a global economy.
3. Eliminating the skills gap.
4. Meeting the need for life-long individual learning.
5. Facilitating organizational learning.

Each of these challenges has potential impact on HRD. Though HRA has had its inception in the 1960s, it is an evolving concept, which is still at nascent stage. Nonetheless, its relevance to organizations is immensely gaining ground. Armed with various measures and figures, managers and firms can focus on decisions regarding investments in areas of intellectual capital that will have the greatest payoff for the firm. Internally and externally, HRA would provide information to investors and other staff, of the value of human resources, the returns on investments in training and development and also the link between HR interventions and financial results. As a way to assess human capital, HRA represents a new way of thinking strategically.

Boudreau has noted that measures of HRA and benefits can serve a variety of purposes. It acts as a catalyst for change. It tends to enhance the credibility of the HR functioning for it was not long back that this function was looked down disdainfully as only a department to organize picnics for its staff. HRA also helps persuade others to support investment in HR and also to improve the quality of HR decisions. Change is taking place at the tremendous rate. To make it effective and in order to make the team, HR professionals need to develop the business skills of strategic planning and process technology. And the first step towards the sustainable growth is accounting HR in financial terms.

### **Investment in Human Resources**

There is much debate as to whether the human resources of an organization can be considered as an asset and treated accordingly in the accounting system. There are two schools of thought. One says that human resource is an asset and the other does not agree with this. Asset is anything which is owned by the entity to derive service in future and should have legally enforceable claim. As such there is no guarantee of deriving benefits from the existing human resources in future and has no sales value like other assets. Therefore, legally, human resource is not an asset claims one school of thought. Besides, company law also does not consider it as an asset. But the other school is of the opinion that the "human resource is an asset". This school of thought puts forth few contentions in favour of its opinion as follows:



- 1) There is a legal ownership on the "human resource" which could in practice prevent him from joining the other organizations unless properly relieved by complying with some formalities like giving advance notice of resignation, etc.
- 2) Uncertainty of deriving benefits is a common problem to all assets, not only with the human resources. Deriving future benefit may be a big question mark in other assets too due to many factors. "Obsolescence" may be the one.
- 3) Generally, an asset needs maintenance and development support from the organization so as to derive benefits over a long period of time. Similarly, human resources as an asset also are in need of training and development in order to maintain the service potential for the employer.
- 4) R.L. Woodruff Junior observed that treating people as assets and accounting them is logical and satisfactory to the expectation of the future economic benefits.

The above view supports that the human resource is an asset as they are valuable resources to an organization and investments in such asset will help organization to improve.

#### **Limitations of Human Resource Accounting**

Human Resource Accounting is the term used to describe the accounting methods, system and techniques, which coupled with special knowledge and ability, assist personnel management in the valuation of personnel in financial terms. It presumes that there is great difference among the personnel in their knowledge, ability and motivation in the same organization as well as from organization to organization. It means that some become liability too instead of being human assets. HRA facilitates decision making about the personnel i.e., either to keep or dispense with their services or to provide training. There are many limitations which make the management reluctant to introduce HRA. Some of them are:

- i) There is no proper clear-cut and specific procedure or guidelines for finding cost and value of human resources of an organization. The systems which are being adopted have certain drawbacks.
- ii) The period of existence of human resource is uncertain and hence valuing them under uncertainty in future seems to be unrealistic.
- iii) There is a fear that HRA may dehumanise and manipulate employees.
- iv) For e.g., an employee with a comparatively low value may feel discouraged and develop a complex which itself will affect his competency to work.
- v) The much-needed empirical evidence is yet to be found to support the hypothesis that HRA as a tool of the management facilitates better and effective management of human resources.
- vi) In what form and manner, their value to be included in the financial statement is the question yet to be classified on which there is no consensus in the accounting profession.



- vii) As human resources are not capable of being owned, retained and utilized, unlike the physical assets, there is problem for the management to treat them as assets in the strict sense.
- viii) There is constant fear of opposition from the trade unions as placing a value on employees would make them claim rewards and compensations based on such valuation.
- ix) Another question is, on value being placed on human resources how should it be amortized. Is the rate of amortization to be decreasing, constant or increasing? Should it be the same or different for different categories of personnel?
- x) In spite of all its significance and necessity, tax laws do not recognize human beings as assets.
- xi) There is no universally accepted method of human asset valuation.
- xii) As far as our country is concerned human resource accounting is still at the developmental stage. Much additional research is necessary for its effective application.

### **Conclusion**

People are the greatest asset the only real difference between one organization and the other is the performance of the people. The survival, development and performance of an organization depends heavily upon the quality of manpower, right from Alfred marshal a century ago, down to the management Guru Peter Drucker, focusing attention knowledge workers and knowledge industries come out clear message that “Knowledge” is the key to development. We are in the knowledge era where the new wealth of matrons is tied directly up with the creation, transformation and capitalization of knowledge. With the concepts of the liberalization, privatization and globalization being applied all over the countries in the world, the need has arisen to go in for quality products and quality service. Each organization has to compete with one another to improve the quality and device cost reduction measures to exist in the industry. That could be done only with the development of human capital. Japan and other East Asian countries like Korea and Taiwan have recorded rapid economic growth, it is only because of their investment in human capital, which cannot be easily measured and which differs from one to another. Basically, when we talk of human capital it refers to the human knowledge, their inner capabilities and creativity qualities. These are to be tapped from the employees. With all the development of technology it cannot be fully utilized to its full potential without knowledge and skill. The capabilities of the human capital in relation to the needs of the organization should be improved with the creation of a climate in which the flower of human knowledge, skill, capabilities and creativity can bloom. How do we develop our human capital and put it to optimum use is the challenge that the present-day corporate sector faces? Technological improvements, business strategies, quality concerns etc., will all have to

be implemented through people (human capital only). So, it is people who make all the difference. People and their development are quite central to meeting the needs of globalization and liberalization. The human capital available in the organization should be rightly assessed and should be further developed through motivation training and perception to the needs of the organization. Only then, the organizational goals can be achieved and more so, it can continue to be market contribution in the field of competition. With the arrival of micro-electronic technology, work processes have changed. The computer technology offers greater precision but demands different skills. The owners (personnel) of these new skills are both technically educated and trained on the job.

It is the human capital, which should be rightly invented for the qualitative improvement of human beings who are considered the most valuable asset of an organization. Human capital refers to the basic skill, capabilities, the perception know-how and expertise. Every individual has certain skills and understanding. The education one has undergone should help him to develop knowledge in general. Till one gets basic employment he is not keen on planning his future and there is uncertainty. As one is placed in an organization in some position, he starts to look for elevation. The organization too would tap his basic skill and capabilities and divert them to achieve the goals of the organization and in the process, it attempts to develop his basic skill through proper training, motivation and direction. The human capital is rightly put through for the personnel in the organization for effective functioning, right decision making and career development. In all these it creates value to the organization and makes it more stable in the competitive environment.

Thus, HRA aims at converting human data into money value. Human data as such has not been accounted for since it is not like a physical asset which has a direct money value whether it is being represented by historical cost or replacement cost or conversion process of human data into money value: Human data has to be identified as the value of the production capacity etc., of the people at work should result in the growth of the organization and in turn the profit and the value of the firm. There are of course different approaches to human resources which work out the human capital into money value. It does not merely into account the present human asset as such but it takes into account the growth of the human asset with reference to the future needs of the organization with the various policy elements and action plan introduced and implemented by the organization.

In India, human resources accounting unit now has not been introduced as a system. So far as the statutory requirement is concerned, the Companies Act, 1956 does not require furnishing of any significant information about human resources in the financial statements of

companies. The existing accounting standards, in the absence of any negative directive, may be seen to support the adoption of human resources accounting by an organization for the purpose of meeting its own requirements. The dichotomy in accounting between human and non-human capital is rather fundamental, while the latter is recognized as an asset and recorded as such in the financial statement, the former is totally ignored. With the accelerated growth in science and technology, the value of human capital is gradually increasing and hence it is essential for a company to reflect the investment in human resources. In the absence of HRA, the management may not realize the negative effects of certain programmes aimed at improving profits in the short run. Such programmes may result in decreased value of human assets due to fall in productivity levels, high labour turnover and low morale.

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