

Human Resource Accounting

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Definition:

Human resource accounting is the process of identifying, measuring and communicating information about human resources which treats people as machines with a monetary value attached to them. According to Flamholtz the definition of HRA is "the measurement and reporting of the cost and value of people in organizational resources".

Importance:

Adam Smith, in his renowned book "Wealth of Nation", classified the factors of production into Land, Labor, and Capital on the other hand the modern management reclassified them as Men, Material, Machinery and Money. The terms 'Labor' and 'Men' have now been termed as 'Human Resource'.

The competitive position of any organization largely depends upon its assets while human being is the most important asset among them. Managers often say that people are their most important asset. Especially in case of IT firms, academic institutions, consulting firms etc., the total worth of the organization depends mainly on the skills of its employees. Without introduction of human being no production is possible, that's why today the importance of human resources as well as development of human resources have been well recognized. Demand of professionally qualified persons has now been increasing worldwide even production workers are required to be skilled not only on the base of experience of years but also knowledge about technical side of production including know how to work with modern and more

sophisticated computer based machinery. Moreover, a person has to know how he can save time and wastage of material in addition to be more productive.

Non-Disclosure in the Balance Sheet:

Instead of so much importance of human resources it is also fact that a balance sheet which is supposed to disclose all the assets of the enterprise completely missing this asset. Human asset is virtually never shown on the face of balance sheet as a distinct category. It seems that economic value of human resources is recognized but off the accounting books. So how an auditor can claim in his report that the balance sheet shows a true and fair view of the business on a specific date. The situation gets more awkward when we see that profit and loss statement accounted for all human resources related costs. The cost of HR encompasses cost of recruiting, selection, contracting, placing, training, orientation, promotion, improvement, substitution, exit rewards, facilities, health, safety, pensions, contributions to social security, retirement, redundancy and dismissal.

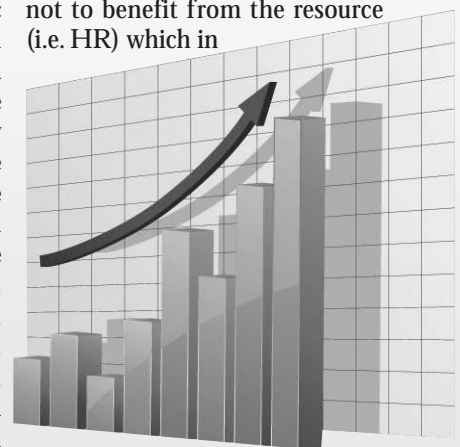
Valuation Problem:

The biggest challenge in HRA is that of assigning monetary values to the worth of employees which may be equally acceptable to all in turn which may be disclosed in the balance sheet. In this regard we can go to the methods developed to appraise performance of individuals. Among number of these methods no one can suggest which method free of major limitations. Because if we assign a value to an employee then it will be based on personal judgment (which may be different among different appraisers even one appraiser may also decide slightly different during different times regarding same person) on the other hand an effective human resources as a team create a synergy effect i.e. $2+2>4$. So researchers are facing a considerable issue to develop a framework model to be used to quantify human qualities into monetary terms which is based on systematic standardized

parameters. Furthermore, this asset cannot be sold therefore there is no independent check of valuation.

Relevant International Accounting Standard (IAS):

IAS 38 deals with the accounting treatment of Intangible Assets, however, states that a resource will be qualified as an asset only after meeting two conditions one of which is control of the entity over the resource, in turn the control may be assumed if entity can legally enforce others not to benefit from the resource (i.e. HR) which in



the use of the entity, similarly an entity has insufficient control due to the absence of any legal or contractual right over the expected future economic benefits arising from customer relationship or customer loyalty. In this way International Accounting Standards Board does not allow an accountant to recognize and disclose HR as an intangible asset in the balance sheet of the entity. Therefore, The Companies Ordinance does not require so, however, some companies in order to maintain good practice disclose HRA or some aspects of HRA in the annual report.

References:

- http://en.wikipedia.org/wiki/Human_resource_accounting
- *International Accounting Standard 38*

