



# HUMAN RESOURCE ACCOUNTING

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## MEANING :

**Human resource accounting (HRA)** is the process of identifying and reporting investments made in the human resources of an organization that are presently unaccounted for in the conventional accounting practice. It is an extension of standard accounting principles. Measuring the value of the human resources can assist organizations in accurately documenting their assets. In other words, human resource accounting is a process of measuring the cost incurred by the organization to recruit, select, train, and develop human assets.

## **DEFINITION:**

- The American Association of Accountants (AAA) defines HRA as follows:  
‘HRA is a process of identifying and measuring data about human resources and communicating this information to interested parties’.
- According to Stephen Knauf, ‘ HRA is the measurement and quantification of human organizational inputs such as recruiting, training, experience and commitment’.

## NEED FOR HRA:

- ❖ 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.
- ❖ 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.
- ❖ 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.
- ❖ 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.
- ❖ 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.

# OBJECTIVES OF HRA:

**Rensis Likert described the following objectives of HRA:**

- Providing cost value information about acquiring, developing, allocating and maintaining human resources.
- Enabling management to monitor the use of human resources.
- Finding depreciation or appreciation among human resources.
- Assisting in developing effective management practices.
- Increasing managerial awareness of the value of human resources.
- For better human resource planning.
- For better decisions about people based on improved information system.
- Assisting in effective utilization of manpower.

# **SIGNIFICANCE OF HUMAN RESOURCE ACCOUNTING**

- It provide a basic platform of planning in that the objectives, aims and methods for acquiring human resources are included.
- It provide various assistance to the management in employment and utilization of human resources.
- It helps the management in planning and executing personnel policies and plans pertaining to the recruitment, transfer, promotion and retrenchment of human resources.
- It helps to study and assessing the inner strength of an organization and helps the management to overcome the most adverse and unfavourable circumstances.
- It helps to analyse the causes of high labour turnover at various levels and taking preventive measures for control over it.
- It helps to give the cost of developing human resources and as such it will enable the management to ascertain the cost of labour turnover also.



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- It helps in evaluating the expenditure incurred for imparting further education and training of employees in terms of benefits derived by the organisation.
- It helps to find out the real cause for low utilisation of HR, under utilisation of assets as well as low return on investment.
- It helps the HR managers for conducts a better ways and means for organisational development in the organisation.
- It helps in improving the efficiency of employees towards improving their performance and their worth.
- It helps the each employee to understand his contribution towards the perspective results of the firm as well as the expenditure incurred by the firm on him.

# **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 organization can select a person with highest expected realizable values.
- Human resource accounting can change the attitude of managers completely, thereby, they would try to maximize the expected value of human resources and effective use of human resources in the organization.
- It also provides necessary data to devise suitable promotion policy congenial work environment and job satisfaction to the people.



# Limitations of HRA:

**HRA is yet to gain momentum in India due to certain difficulties:**

1. 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.
2. There are no standardized procedures developed so far. So, firms are providing only as additional information.
3. Under conventional accounting, certain standards are accepted commonly, which is not possible under this method.
4. 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.
5. It is believed that human resources do not suffer depreciation, and in fact they always appreciate, which can also prove otherwise in certain firms.
6. The lifespan of human resources cannot be estimated. So, the valuation seems to be unrealistic.

# **Methods of Human Resource Valuations**

- ❖ Historical Cost Method**
- ❖ Replacement Cost Method**
- ❖ Economic Value Method**
- ❖ Standard Cost Method**
- ❖ Present Value Method**
- ❖ Current Purchase Power Method**
- ❖ Opportunity Cost Method**

## **Historical Cost Method:**

This method is based on costs incurred on recruitment, training, familiarization etc. It is developed by Rensis Likert. This is a very simple method based on traditional principles of accounting. Under this method an attempt is made to have a proper match between cost and revenue.

The plus point of this method is that the organization can show the value of human capital in its balance sheet and profit and loss account, the weak point of this method is that it fails to fulfill the need of developing a system of HRA based on systematic valuation of human resources.

## **Replacement Cost Method:**

Under this method the replacement cost of existing personnel is estimated. Replacement cost includes the cost of recruitment, training and opportunity cost for the intervening period. This serves the purpose of making valuation of human resources periodically. It helps in planning for human resources in future. The difficulty in this method is that the value differs from person to person making it difficult to find identical replacement of the present human assets.

### **Economic Value Method:**

The payment made to the human resources till their retirement are calculated and appropriately discounted to get their present economic value.

### **Standard Cost Method:**

This method is in improvement over replacement cost method. Under this method the standard costs of recruitment, training and development are developed and established every year to overcome complications in calculations. These costs represent the value of human resources for accounting. It is easy for implementation and control.

### **Present Value Method:**

Under this method the net contributions of employees to the earning of the organization are discounted to have present value of human resources.

### **Current Purchase Power Method:**

In this method the historical costs are converted into current purchasing power of money with the help of index numbers.

### **Opportunity Cost Method:**

Under this method the value of human asset is determined in their alternative use or the next best alternative use. This value forms the basis for valuation of human asset of organization. For calculation of opportunity cost bidding method is used. But it is difficult to decide bid or offer.



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