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A Study on “The relevance of Human Resource Accounting in the Present Scenario”

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ABSTRACT

The past few decades have witnessed a global transition from manufacturing to service based economies. The fundamental difference between the two lies in the very nature of their assets. In the former, the physical assets like plant, machinery, material etc. are of utmost importance. In contrast, in the latter, knowledge and attitudes of the employees assume greater significance. Hence, the success of these organizations is contingent on the quality of their Human Resource- its knowledge, skills, competence, motivation and understanding of the organizational culture. This paper reviews the state of the art of the development of HRA in the present scenario and its relevance in industry. The paper assesses contributions and categorizes them according to studies which 1. Some basic assumptions for HR valuation, 2. Present empirical evidence, case and field studies on the various methods of reporting human resource assets and implementing HRA in various organizations, 3. Analyze methods for measuring human resources, 4. The purposes of HRA in an organization, 5. Valuation methodologies of Human Resource Accounting, 6. Problems and Limitation of HRA, and 7. The findings on “HRA, human capital value chain”. The paper draws conclusions on the state of the HRA and suggests recommendations based on the study.

Keywords : Human capital, Return of Human capital, Return on Knowledge,

Introduction:

The past few decades have witnessed a global transition from manufacturing to service based economies. The fundamental difference between the two lies in the very nature of their assets. In the former, the physical assets like plant, machinery, material etc. are of utmost importance. In contrast, in the latter, knowledge and attitudes of the employees assume greater significance. For instance, in the case of an IT firm, the value of its physical assets is negligible when compared with the value of the knowledge and skills of its personnel. Similarly, in hospitals, academic institutions, consulting firms etc., the total worth of the organization depends mainly on the skills of its employees and the services they render. Hence, the success of these organizations is contingent on the quality of their Human Resource- its knowledge, skills, competence, motivation and understanding of the organizational culture.

In knowledge-driven economies therefore, it is imperative that the humans be recognized as an integral part of the total worth of an organization. However, in order to estimate and project the worth of the human capital, it is necessary that some method of quantifying the worth of the knowledge, motivation, skills, and contribution of the human element as well as that of the organizational processes, like recruitment, selection, training etc., which are used to build and support these human aspects, is developed. Human resource accounting (HRA) denotes just this process of quantification/ measurement of the Human Resource.

Some basic assumptions for HR valuation

Each employee's cost to company (CTC) should be forecasted and discounted back separately. Thus a separate database comprising compensation details, age and experience details, historical promotion pattern for each employee should be constructed. The database serves as a powerful MIS tool for value interpretation. The growth rate of earnings of each employee till retirement should be determined for projecting the CTCs after looking into the company's compounded annual growth in CTC's for different employee classes, global

industry trends for the future (e.g., what happens after 5 years when the demand for Y2K jobs in the software sector obliterates), and sustainable growth rates for the next 25-30 years given the nominal interest rates of the Indian economy. The attrition rates for the company / industry should not be considered as a deduction factor, as the employees who leave the company will be replaced by others to maintain the level of operations, and thereby the employee strength remains unchanged (conservation of employee stock / inventory). This is also consistent with the going concern concept.

Objectives:

1. To study and redefine the concepts, objectives and role of Human Resource Accounting in Human Resource Management
2. To understand the measurements of Human Resource Capital, Costs and Value
3. To understand basic assumptions for HR valuation
4. To relate HR capital, cost and value with employee retention, customer retention and profitability

Need for the study:

The present study throws light on human resource accounting, human resource cost, value and capital. It is so imperative from the point view of corporate brand image, retention of employees and customer satisfaction and retention. Customer retention drives customer profitability and the good return on investment to the company. Hence, it is helpful to understand the in and out of Human resource accounting.

Methodology:

Both primary and secondary have been used in the study. As per primary data is concerned, HR managers, accounting officers, trainers, campus recruiters and employees of Xchanging solutions private ltd, Shimoga, IcfaiBusiness Academy -Bangalore and HDFC bank of Shimoga branch are personally met and gathered the required information and secondary data of those companies which follow the basic premises of Lev & Schwartz model for valuing their human resources of

a company after parallel ascertaining a human organizational inventory to assess the effect of qualitative human variables (e.g., employee job satisfaction, 360 degree peer evaluation, etc.) on HR value considered in the study.

Literature Review:

Arnold H.J. & Feldman D.C.'s article of 'A multivariate analysis of determinates of turnover' published in Journal of Applied Psychology analysis the different determinants of employer attrition. Arthur J.B.'s article 'Effects of human resource systems in manufacturing performance and turnover' published in 'Academy of Management Journal depicts the correlation between employee turnover and their working performance in manufacturing unit. Bartel A.P. points-out in the importance of training and development to gain morale among the employee and result of it in the article 'Productivity gains from the implementation of employee training programs' which published in the journal of Industrial Relations.

Findings:

Following are the major findings of the study;

1. Throughout the globe, the knowledge has become the key determinant for success of economy and business, but most of the Indian companies have been focusing on 'return on investment' rather than 'Return on knowledge'.
2. There is a need to measure the abilities of employees at every level of the hierarchy to create value from their knowledge and ability.
3. The current accounting system is not able to measure the actual value of employee's capabilities and knowledge.
4. As each year the cost on human resource development increases, hence it indirectly affects future investments of a company
5. HRA system helps in a variety of managerial decisions like recruitment planning, attrition analysis, personnel advertisement analysis, return on knowledge and capital budgeting which will help to save a lot of trouble in the future.
6. Like any accounting exercise, the HRA too depends heavily on the availability of relevant and accurate information relating to HR.
7. HRA is essentially a tool to facilitate better planning and decision making based on the information regarding actual human resource cost and organizational returns.
8. Information on the tangibles like intellectual capital becomes necessary to measure the true worth of the organization. This information, thought unaudited, needs to be communicated to the board and the stockholders.
9. The HRA valuation is important for decision making in order to achieve the organizational objectives and to improve the output.
10. When proper valuation and accounting of the human

resources is not done, then the management may not be able to recognize the negative effects of certain programs, which are aimed at improving profits in the short run. If not recognized on time, these programs could lead to fall in productivity levels, high turnover rate and low morale of existing employees.

11. In addition to being fairly compensated, employees of an organization place high value on:
 - a. Being in an environment where they can grow, learn and advance themselves in the ladder of the hierarchy
 - b. The managerial skills and abilities of their immediate supervisor
 - c. Being treated fairly, appreciated and acknowledged
 - d. Doing work that makes a contribution
12. These determinants of employee satisfaction drive employee retention in an organization
13. The retention rate among the key employees drives customer satisfaction
14. Customer satisfaction drives customer retention
15. Customer retention drives profitability and other measures of financial performance including total stockholder return.

Conclusions:

A growing number of studies have attempted to show the link between human resources and performance. We believe that though the case is not watertight, due to a number of methodological reasons, the weight of evidence is beginning to look compelling. An important finding of this research is that both contingency and best practice models can complement each other to create the conditions for effective human capital management. That is, the adoption of such high performance practices as incentive-based pay or selective staffing is part of building HR architecture. The details of how these practices become effective within the organization, and then becomes a matter of aligning these broad principles to the strategy and the context of the company. There is a now a growing body of work that argues for a convergence between the two views. We believe that greater understanding as to how these two approaches come together to enhance our knowledge of how human capital management can lead to improved competitiveness.

We depict that human resources, both as labor and as a business function, have traditionally been viewed as a cost to be minimized. At best, human resources are viewed as contributing to the efficiency of the organization, but not explicitly as a source of value creation. The rise of human capital management, alongside its relatives the resource-based view and strategic human resource management, has seen this view change dramatically. If human capital really is at the center of competitive advantage, investors may wish to see rather more disclosure in the future.

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