

Human Resource Accounting - A Tactical Use of Lev & Schwartz Model

Dr. Zine Dyandev Eknath

HOD Economics

Arts , commerce & Science College, Sonai

Tal.- Newasa , Dist.- Ahmednagar (MS)-414105

Email:- dnyandev79@gmail.com

Abstract

HRA has been defined by American Accounting Association's committee –"HRA is the process of identifying & measuring data about human resources & communicating this information to interested parties". Stephen Knauf defined HRA as "The measurement & quantification of human organizational inputs such as recruiting, training, experience & commitment." According to Eric G. Flamholtz HRA represents-"Accounting for people as an organizational resource. It is the measurement of the cost & value of people for the organization". Hence, it can be said that, it is the process of developing financial assessment for people within organization & society & monitoring of these assessment through time, it deals with. Although HR valuation has important implication for external financial reporting, in the contemporary economic scenario valuing HR has been greater significance for internal HRM decision.

Keywords:-Accounts, Human, measuring, training

Introduction:-

Human is the core factor and which is required to be recognized prior to any other 'M's. But till now an urgent need based modification is required while identifying and measuring data about human resources. In this paper my objective is to identify the extensive use of Lev & Schwartz model of Human resource accounting, in spite of several criticisms from various sides regarding its applicability. Further more, it also portrays the applicability in wide variety of organization of such model (some public sector units and IT based sector).

Human is the buzzword in the modern knowledge based society. It is the most vital input on which the success & failure of the organization very much depend upon. Starting from the classical economist to modern human capital economist such development is considered to be a continuous process.



It is one of the most important 'M' associated, which is considered while taken care of 4M's associated with any organization and they are money machines, materials and men. But the most interesting thing is that the first three are recognized and find a place in the assets side of the Balance sheet of the organization. But in case of fourth one ambiguity prevails among the accountant. In spite of its usefulness has been acclaimed in various literature over the decades but its application still remain a suspectable issue, the IASB and the ASB in different countries have not been able to formulate any specific accounting standard for measurement & reporting of such valuable elements.

It is a popular phenomenon among the Indian corporate world is to disclose information relating to human resource in annual statements. In this context, it is necessary to conduct a study to assess the disclosure pattern of HRA information in Indian corporate World.

It first promulgated by BHEL (Bharat Heavy Electrical Ltd), a leading public enterprise, during the financial year 1972-73. Later it was also adopted by other leading public and private sector Organization in the subsequent years. Some of them are Hindustan Machine Tools Ltd.(HMTL). Oil and Natural Gas Corporation Ltd.(ONGC), NTPC, Cochin Refineries Ltd. (CRL), Madras Refineries Ltd.,(MRL), Associated Cement Company Ltd.(ACC) and Infosys Technologies Ltd.(ITL).

However, adaptability of various model (mainly Lev and Schwartz model,

Flamholtz model and Jaggi and Lev model) and discount rate fixation and disclosure pattern ie. either age wise, skill wise etc in BHEL, SAIL, MMTC (Minerals & Metals Trading Corporation Of India Ltd.) HMTL, NTPC make it clear, that there has been no uniformity among Indian enterprises regarding HRA disclosure.

Meaning of Human Resource Accounting:-

HRA has been defined by **American Accounting Association's committee** – "HRA is the process of identifying & measuring data about human resources & communicating this information to interested parties". Stephen Knauf defined HRA as "**The measurement & quantification of human organizational inputs such as recruiting, training, experience & commitment.**"

According to Eric. G Flamholtz HRA represents- "**Accounting for people as an organizational resource. It is the measurement of the cost & value of people for the organization.**"

Hence, it can be said that, it is the process of developing financial assessment for people within organization & society & monitoring of these assessment through time, it deals with.

Although HR valuation has important implication for external financial reporting, in the contemporary economic scenario valuing HR has been greater significance for internal HRM decision.

Problem Statement:-

Understanding the way of valuation of human resources by using **Lev & Schwartz model** and how valuation of such asset are related with the other financial variables for financial reporting purpose

Research Objectives:-

The main objectives of the study are:

- i) To assess the way of presenting HRA information in the financial statement by selected companies
- ii) To identify HRA methods and models (mainly **the extensive use of Lev & Schwartz model**) which are used to arrive at human resource value.
- iii) How human resource are related with the other accounting variables for the purpose of human financial reporting in selected companies.

PRODUCTIVITY & PERFORMANCE INDICATORS:-

| Name | HR/TA | HR/FA | Turn/HR | VA/HR | PBT/HR | HR/VA | HR/No of employee |
|---------|-------|-------|---------|-------|--------|-------|-------------------|
| BHEL | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | - |
| SAIL | - | - | - | - | - | - | - |
| MMTC | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | - |
| ONGC | - | - | - | - | - | - | - |
| NTPC | ✓ | - | ✓ | ✓ | - | - | - |
| INFOSYS | - | - | - | ✓ | ✓ | ✓ | ✓ |

Source: Secondary

Terminology used:

- 1) PBT-Profit Before Tax
- 2) HR- Human Resource
- 3) TA-Total Assets

- 4) Turn-Turnover (or Sales)
- 5) FA-Fixed Assets
- 6) VA- Value Added

Models of Human Capital Valuation:-

Many models have been created to value human capital. Some are based on historic costs while some are based on future earnings. But each has its own limitations and one model has proved to be more valid than other. Although the **Lev and Schwartz model** has been the most widely use model for its ease of use & convenience.

The Lev & Schwartz Model:-

The **Lev and Schwartz model** states that the human resource of a co is the summation of value of all the Net present value (NPV) of expenditure on employees. The human capital embodied in a person of age r is the present value of his earning from employment

Under this model, the following steps are adopted to determine HR Value.

- i) Classification of the entire labour force into certain homogeneous groups like skilled, unskilled, semiskilled etc. and in accordance with different classed and age wise.eg. In Infosys the classification is based on software professionals & support staff etc.
- ii) Construction of average earning stream for each group.eg. At Infosys Incremental earnings based on group/ age have been considered.
- iii) Discounting the average earnings at a

predetermined rate in order to get present value of human resource's of each group.

iv) Aggregation of the present value of different groups which represent the capitalized future earnings of the concern as a whole,

$$V_r = \frac{I(t)}{(1+r)^{t-r}}$$

Where, V_r = the value of an Individual r years old
 $I(t)$ = the individual's annual earnings up to retirement
 t = retirement age
 r = a discount rate specific to the cost of capital to the company.

Critical appraisal of the Lev & Schwartz model: –

- 1] It is essentially an input measure .It ignores the output i.e. productivity of employees.
- 2] Service state of each individual employee is not considered.
- 3] The training expenses incurred by the company on its employees are not considered.
- 4] The attrition rate in organization is also ignored.
- 5] Factors responsible for higher earning potentiality of each individual employees like seniority, bargaining capacity, skill, experience etc. which may cause differential salary structure are also ignore.

Conclusion:-

The conceptual thinking about valuation human resources is still in a developing stage. No model of HR accounting is accepted by the accounting bodies all over the world. However, still we find some application of **Lev & Schwartz model** is most public sector units and IT based sectors. In knowledge based sectors where human resources are considered to be the key elements for monitoring the business activities to attend their goals successfully, may not overlooked this side. Hence, considering the great significance of HRA proper initiation should be taken by the government along with that other professional & accounting bodies both at the national & international levels for the measurement & reporting of such valuable assets.

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