CHAPTER - ONE

INTRODUCTION
The Issue

One of the major purposes of annual financial reporting, particularly for not-for-profit organization, is to provide information for evaluating the effectiveness of the management of resources in achieving organization's goals. Again, "performance measures should be quantified in terms of identified goals". In case of business organizations the basic objective is to earn profit through employing resources, while in case of nonprofit organizations like charitable institutions, the primary objective is to provide services through the effective use of resources provided by the funding agencies. Profits earned and services rendered are the outcome of effective utilisation of resources employed for the purpose. Accounting aims to report them periodically. Hence, to have a clear idea about how much of the objective of an organization has been achieved requires a precise but important information on both profits earned or services rendered and resources utilised for the purpose. Income Statements and Balance Sheets are designed to reflect the annual earnings and resource position at the year end. It is generally inferred that income is the outcome of resources. In other words, income is the flow and resources are the sources of such flow. Which is why, through calculating return on investment (ROI) we can derive the rate of return on such resources. Usually land & building, plant & machinery, inventories and monetary claims are traditionally considered as resources. But they themselves cannot generate goods or services. It is men with the help of whom these assets can be operated. In fact, they are the catalysts of the production process. More the efficient

the employees, more the rate of earning. Paradoxically, value of such human resources (HRs) are not conventionally reported in our financial statements. Even the expenses incurred for the selection, recruitment and training with a view to acquiring and developing such resources for deriving services from them are neither capitalised nor amortized in the books of accounts. That is why developed the concept of human resource accounting (HRA). In absence of reporting the value of these HRs the complete financial picture of profit earning and the sources of such earnings of a profit seeking organization is not available.

The problem is aggravated further in case of nonprofit organizations (NPOs), where the primary objective, it is mentioned earlier, is to render services to the society with the help of resources used for the purpose. The basic objective of reporting here should be providing information on the services rendered by it and its efficiency and effectiveness in providing those services. Measurement of effective use depends on two factors: one, services rendered and two, resources used for the purpose. The present accounting system does not make provision for supplying complete information on both of the two. Here services are not measured and resources engaged in generating the services are not fully reported. In fact, in a NPO, some people come together, collect some donations and volunteer their labour to render services.

3. Nonprofit organizations range from large and complex to the small and simple ones. They include hospitals, colleges and universities, religious organizations, associations, foundations, cultural institutions and the voluntary social service organizations. The features of the nonprofit organizations have been discussed in detail in Chapter-III. Voluntary social service organizations are selected for our study, since in this area whole hearted involvement of HRs is indispensable for achieving the objective of such organizations.

usually at free of charges\textsuperscript{5} or at a minimum rate to the members of the society. The resources available here through donations, contributions etc. is not of primary considerations. The people associated with these entities volunteer their services usually benevolently or in exchange of a token salary. The magnitude of services which a NPO provides, depends on the generosity of these people. That apart, in case of profit seeking organizations, an argument though not so plausible, may be given in support of non-disclosure\textsuperscript{6} of the value of HRs. Existing set of employees may be easily replaced by another without incurring heavy expenses, and without compromising considerably the primary objective of earning profit. It is so because, in perfect competition the marginal revenue available from the services of an employee is assumed to be equal to wages payable to him. But this argument does not hold good for a NPO, in general, and for charitable institution, in particular where the basic objective is to generate and distribute services to the weaker section of the society. Moreover, in such cases, the role of its physical and monetary assets in relation to its associated people is very insignificant. The basic objective of providing services cannot be fulfilled without the whole-hearted labour of the people associated with the NPOs. That is why reporting of the values of HRs is of much significance in case of NPOs. But the conventional accounting system makes provision neither to report the value of services derived from them, nor the information on the value of those human resources. The traditional system usually aims to reflect how far the restrictions imposed by the resource providers are adhered to\textsuperscript{6}. Hence, it appears that the objective (of financial reporting of a


NPO) of reporting the services rendered by it and its effectiveness in the use of resources is not fulfilled to a considerable extent.

With a view to bridging the gap between what is expected of accounting system of a NPO and what is actually provided by the conventional accounting practices in this area, the services rendered by the organization should be valued and reported. Moreover, the value of human resources, the primary source of such services, should also be accounted for. Services rendered to society by NPO, in fact, flow mainly from HRs. Measurement of a flow cannot be completed unless its origin, or source is accounted for. The traditional accounting system of NPO makes provision for measuring and reporting neither the flow of these services nor the stock or sources of such services. The present study is an humble approach to find out a solution, if possible.

I

The Objective of the Study

Machines and materials together in an organization can produce nothing without help from human hands. The greater the efficiency of the human forces, the greater the profit earning capacity of a firm. Generally, the performance of an organization depends very much on the behaviour of the human forces it acquires. But that is not reflected in the conventional accounts. The situation is more serious in case of NPOs. While the ultimate goal of the profit organizations is to earn profit for individuals, the objective of NPOs is to provide social services without any intention of realising profit. Thus, generation and distribution of

services rather than earning of profit is the primary objective of the NPOs. Here, the services rendered and sacrifices made by the HRs are far more important than expenses made on office and administration. It is so because they are set up with the basic objective of providing services to the society through their personnel who volunteer their labour for the cause of the society. For instance, Rama Krishna Mission, Bharat Sevashram Sangha and similar other voluntary and welfare organizations in India have been set up with the basic objective of providing services to the poor usually at free of cost.

Therefore, the objective of accounting of NPOs should not be to measure how much physical wealth is at their disposal; rather it should extend to reporting the services rendered by the personnel in the organization who have dedicated their lives for the cause and betterment of mankind. In fact, the latter should be given precedence to the former. It is also worth mentioning here that, there are various types of organizations like governments, local self-governments, voluntary organizations, clubs, hospitals etc. which are established with the objective of rendering social services rather than earning profit. The accounting system of all of them, however, are not identical. Of course, there is one thing in common among them. In all cases, the objective is to report whether the funds entrusted to these entities, are utilised according to the restrictions imposed on them by the funding agencies or resource providers. That is why, respective accounting frameworks have been geared to what is popularly called, "Fund Accounting". Here the principal objective of accounting is to guard against any probable fraud and misappropriation of funds. Even though the present system is capable

of accomplishing their objectives, it fails to show how efficiently the resources are utilised. Here neither return of capital, nor return on capital should be the basic thing to be reported. On the contrary, the information on the quantum of the services expected to be derived from the people involved in the entity can serve the donors better in their decisions as to the amount they will contribute in future. Hence, the role of HRs, in comparison to other assets in NPOs is far greater than that in POs. The other important point is that, so far as this author's knowledge goes, none of the institutions reports in their financial statements on the value of HRs employed in those organizations.

The present study attempts to study the accounting system of one category of NPOs, namely the charitable institutions, and tries to account for the HRs involved in organization. Hence, the objective of the study may be summed up as follows:

(i) To measure the values of HRs engaged in a NPO.
(ii) To examine the position of the value of HRs in relation to other assets in a NPO.
(iii) To highlight the contributions to society made by the dedicated people of the organization.
(iv) To evolve an index of performance of a NPO in terms of accounting indicators.
(v) To estimate the relative contributions to the society made by the funding agencies and the people serving the NPO, and ultimately,
(vi) To devise a system of accounting for a NPO, so that the extent to which the basic objective of the organization for which it is meant for can be presented in the annual accounting statements.
Research Methodology

The whole exercise accomplished in this study is more or less conceptual. The study neither aims to develop a new theory of HRA nor aspires to modify what has been previously known on the subject. It has attempted to apply to a NPO a popular HRA model which is usually applied to POs.

Since the inquiry basically aims to apply HRA models to NPOs, the study has restored to a two-pronged approach in solving the problem. On the one hand, it has made a discussion at the theoretical level on the development of major HRA models, their relative merits and demerits and the problems involved in measuring the value of HRs as per the models. An accounting model has also been suggested to reflect the accomplishment of the objectives of a NPO for which it is set up. On the other, an attempt has been made to apply one important HRA model, the application of which seems feasible. With a view to have an empirical verification of the model, a NPO has been selected for our study.

The Rama Krishna Mission Hospital and charitable unit, both under the supervision of Rama Krishna Mission Boys' Home, Rahara, North 24-Parganas, West Bengal, India, are considered for our study. The financial reports of the organization are considered and through administering questionnaire various bits of information are collected for human resource accounting. Then an attempt has been made to integrate the financial report and the HRA according to the proposed accounting model. For the purpose a comparative analysis between the present and the proposed accounting system is made through some accounting ratios based on the proposed accounting statement. Lastly, an attempt has been made to
highlight how the proposed accounting system can supplement the existing 
system to portray the achievements of the basic objectives of a NPO for 
which the same has been set up.

III

The Scheme of Work

The work comprises of seven chapters. Chapter One, by way of 
introduction, endeavours to highlight the various problems which are not 
encountered by the conventional accounting practices in NPOs. The 
objective of the present study, the research methodology and the scheme of 
work are also discussed in this chapter. While the following five chapters 
are engrossed in the conceptual discussions and empirical verification on 
HRA in NPOs, the last one is engaged in concluding the study.

Since the enquiry basically aims to account for HRs of NPOs, the 
study comprises of conceptual discussion supported by empirical 
verifications. Having considered the historical developments of the 
concepts on HRA, Chapter Two has briefly presented the major HRA models 
enunciated by various authorities and ultimately has selected one of them 
which appears to be appropriate for empirical study in the present 
context.

Chapter Three makes an attempt to analyse the various aspects of 
NPOs. In doing so, it examines the features of these organizations, 
studies their impact on accounting practices, highlights the existing 
objectives of accounting of such organizations and compares between 
conventional accounting principles of NPOs and the POs and presents an 
outline of the existing practices in NPOs.
The question that whether or not the existing accounting system of NPOs is geared up to provide sufficient and useful information according to their objectives, has been thrashed out in Chapter Four. It attempts to develop an accounting model which may supplement the existing accounting system of NPOs to provide necessary information in respect of the services rendered by the employees, the contributors and also by the organization itself. This is for identifying how much of the objectives for which the NPOs have been established has been achieved.

The accounting model, as proposed in the previous section requires empirical verification. It has been applied to a NPO, namely, the Rama Krishna Mission Boys' Home, Rahara. The hospital and charitable unit run by the organization is the object of our study. Chapter Five thrives for applying the model to the above charitable unit to test the outcome of the model.

After considering the conceptual aspects of accounting framework of NPOs, the study attempts to value the services of the dedicated personnel. Chapter Six seeks to measure the value of these HRs based on the model proposed by Baruch Lev and Aba Schwartz, since this model is widely accepted. In recent days this method of valuing HRs is considered appropriate by the POs.

By way of summarising what has been done in the earlier chapters, the last one i.e. Chapter Seven is engrossed in concluding how the proposed model will act as a supplement to the existing system with a view to indicating how far the basic objective for which the NPOs are established has been achieved. It also points out some related areas where further investigation is warranted.