6.1 PROBLEMS OF HRA IN INDIA

The expectations from the HRA are great, varied and diverse. HRA has achieved success in many spheres. But they are not free from problems and limitations.

Some of the important problems faced by the HRA are as follows:

1. Implementation of HRA Practices Even after serious efforts made by the researchers and professionals the world over for almost half a century, and for about 35 years of its commencement in India, only five public enterprises ONGC, HPCL, CCI, KRL & OIL are following human resource valuation and accounting practices. No regulatory body or accounting standard formulating body has ever prescribed a reasonably acceptable accounting standard for the valuation and reporting of human resources.

2. Human Resource Accounting Stage In the last 50 years of the journey, human resource accounting has seen a number of changes and faced a lot of controversy. The general accounting practitioners still do not accept HRA as a full proof fully developed system.

In spite of its existence as a concept, the human resource accounting is still in its infancy.

3. HRA Reporting Aspect Deteriorated In India, the practice of HRA is more recent. The first initiation in this direction came from the public sector giant BHEL, which started the human resource valuation and reporting practice from the financial year 1974-75. It was followed by SAIL, NTPC, KRL, HSL, HPCL, ONGC, HMT, CCI, MMTC etc.
Currently only five public enterprises ONGC, HPCL, CCI, KRL and OIL are following the HRA practices. This indicates the deteriorated aspect of HRA reporting practices followed by public enterprises in India at present.

4. **No Standardized Reporting Practices** Due to the lack of standardized reporting practices, human resource value and efficiency and productivity disclosures are hardly comparable among public enterprises in India.

5. **HRA Disclosure and Shareholders Expectations** The study brought to light that unorganized and unregulated disclosure related to HRA do not quite meet the decision maker’s expectations and creates problems for investors in decision making.

6. **Variables Disclosed** The differences in number of voluntarily disclosed variables made it difficult to interpret the information in proper context as the human resource valuation and disclosure practices made it difficult for the users to retrieve the required information for decision makers.

Out of 18 variables, HPCL reported 10 variables, ONGC reported 9 variables, CCI reported 7 variables, and OIL had reported 4 variables while KRL reported only 2 variables among public enterprises under the study. At present ONGC had reported 9 variables, HPCL 10 variables and CCI had reported 7 variables. While, KRL and OIL had stopped reporting HRA. This indicates the poor reporting of variables by public enterprises following HRA at present.
7. **Uncertainty of Human Resource Period** is one of the issues as human resources are uncertain and hence, valuing it under conditions of uncertainty in the future, seems to be practically unrealistic. The contribution of employees are quantified and priced in HRA, determination of the probabilities of their future contribution is a difficult task.

8. **Amortization of the Value of Human Resources** Issue related to amortization of the value of human resource is, what should be the rate of amortization? Whether it should be decreased, kept constant or increased.

9. **Human Resource Knowledge & Estimates** Knowledge of individual human resource could also affect employee bargaining power, both within and outside the enterprise. Employees job satisfaction, growth and stability, have to be ensured, irrespective of the extent and nature of cost to the enterprise. HRA requires information of such variables whose estimates are realistically made.

10. **Valuation of Human Assets** Most of the public enterprises in India valued human assets on the present value of the individual’s future earnings. However, placing an amount or value on the individual’s might offend them, and that it was unethical. Further, assigning a definite value to each individual may not be proper because the knowledge of each individual differed from that of another.

11. **Companies Act 1956** One of the major reasons for not adopting HRA was that the Companies Act, 1956, did not have a provision for the inclusion of human assets value in the financial statements.
There is no statutory requirement under the Companies Act, 1956. Moreover, there was no legal requirement for Indian companies to publish their HRA information, due to the absence of a prescribed format and guidelines. The awareness level of this concept seemed to be very low. Further, it is found from annual reports that the HR departments of some companies in India were reported to be completely unaware of this concept and its utility.

12. **Models Used for HR Valuation** Till date, a number of models for monetary as well as non-monetary valuation of human resources have been developed and suggested but still one does not find a generally accepted approach, as all the models/approaches for valuation have their own limitations.

The biggest challenge in HRA is that of assigning monetary values to different dimensions of HR costs. It was observed that mainly there are two approaches of HRA. Monetary Measures and Non-Monetary Measures.

In monetary measures there are three valuation methods – cost, economic & behavioral method.

All the models emphasis only few aspects and none of these models appear to be having the qualities to enable to fit into all situations and varied organizations.

One of the main reasons that prevented HRA from gaining popularity is the need for objectivity in the HR models. All the models were subjective and were based on several assumptions. Assumptions like an employee would remain in
the same position throughout his tenure in a company and
that the total earnings of a group of employees could be
used to calculate the average earning of an employee, had
obvious flaws. So, this ‘average’ did not reflect the
capabilities and knowledge of an employee. This approach, it
was feared, might result in underestimation of some efficient
employees and over-estimation of some others.

13. **Difficult to Make Comparison Between Two Public Enterprises** In the study it was found that, various public
enterprises used various models of HRA and that comparing
two public enterprises using two different models would be
difficult.

R. Narayanaswamy, Professor (Finance & Control), IIM
Bangalore, Commented:

“There could be concern for the credibility of numbers
reported”. Some analysts also felt the companies could
misuse HRA to enhance their image.

Bharati Gupta Ramola, Senior Director, Price Warehouse,
explained, “A company could use this information to prop up
its image in the investors mind, and change assumptions, to
keep the value positive”. Therefore, care must be taken to
ensure that it is an honest experience.

14. **Creation of Human Assets** Creation of human assets
depends on the relative wage structure, labour market
conditions prevalent and other economic, political and social
factors affecting the mobility of labour force and their effects
on wage negotiation.

In fact, it has been really difficult to assess the relative
contribution made by human beings of an organization using
a mix of resources – physical, financial and human. (P. Mohan Chandran, ICFAI Centre for Management Research, an affiliate of the ICFAI University).

15. **No Accounting Standards Yet** Though the Accounting Standards Board of the ICAI has brought out accounting standards on most of the important areas in accounting and had ensured their implementation by making accounting standards mandatory.

Since the ICAI, the apex body in the accounting profession in India awards the shield and plaques for the best presented published accounts, considering HRA as one of the criterion. So, it should also lay down guidelines for accounting and valuation.

The most regretting fact is that ICAI has not been able to bring any definitive accounting standard on measurements and reporting of human resource cost and value.

The non-disclosure of HR accounting information in financial statements distorts net income disclosed by P & L A/C, a total asset figure in balance sheet and also distorts computation of rate of return on capital employed because its components namely net income and total assets are distorted.

The result of non-disclosure of human resources cost and value information in financial statements do not reveal any quantitative information on human resources side and the statements of affairs is improperly reported to different authorities.
16. The output of HRA information system can be used to take a variety of managerial decisions in the area of human resource management. The accounting managers, associated with the design of HRA system, feel that measurement levels, is the most important problem area. The inability of HRA systems to get integrated with the framework of traditional accounting is also considered to be one of the important problems.

17. **HRA Not Considered as an Integral Part of Accounting System**

HRA has been reported by these public enterprises as supplementary information in the annual reports and is unaudited. The value assigned to the human resources has not been depicted, in the financial statements. So, HRA has not been considered as an integral part of the accounting system.

18. **Different Discount Rates** All the public enterprises used different discount rates for the purpose of calculating the present value of future earnings of employees. Discount rate used for valuation of human resource value is disclosed only by ONGC, HPCL and KRL.

ONGC – Discount rate for 2002 to 2008 is constant 8%, while in the year 2009 it is 7%.

HPCL – Discount rate for 2002 is 12%, 2003 to 2005 is 11%, 2006 is 8%, 2007 Not reported, 2008 & 2009 is 8%.

CCI - Not reported.

KRL - It is constant from the year 1999 to 2005, which is 9%.

OIL – Not reported

It is found that ONGC & HPCL had variable discount rate, while KRL had used constant discount rate.
Any of the Indian public enterprises had not disclosed the appropriate reason for considering specific discount rate for human resource valuation.

Such arbitrary use of different discount rates is a debatable point.

19. **HR Valuation & Tenure of Employees Changes in Organization** The calculation of the probability of an employee’s tenure in the organization and the probability of his promotion to higher ranks is bound to be subjective. As the human resources are highly dynamic, it is difficult to predict with certainty their tenure and promotability.

20. **Social Account & HRV** The companies such as ONGC, SAIL, MMTC, OIL, EIL and CCI, which have also reported ‘Social Accounts’ in their annual reports show the value of human resources both on the assets as well as on the liabilities side of the Social Balance Sheet. This means that their net value is zero.

Moreover, if we consider the recruitment, training and development expenses incurred on employees in the past, their net value to the organization becomes negative.

21. **Accounting Principle & HR Value** Though these organizations have valued their human resources and have reported such values in their annual reports. But is has not been mentioned as to how they are treating the huge expenses incurred by them on hiring, training and developing their employees.

Obviously, they are charging such expenses wholly to the profit & loss, which is against the accounting principles.
22. **Factor Affecting HR Valuation**

- **Employees Classification** Practically all employees are not equally competent enough or skilled in all work, so it is natural that there is a classification of employees into a number of grade/categories based on type of work, experience, classification etc.

It is necessary to note that too many classifications would only complicate the valuation process of human resources.

- **Employees Compensation** At the time of valuation of human asset employee’s compensation package is also an important factor in determining the quantum of asset.

Since compensation packages vary from year to year in each grade, it is necessary for the sake of convenience to keep the average salaries constant over the period of calculation.

- **Weight age Factor** It is well known fact that efforts put in by an employee is not same throughout his tenure in an organization.

- **Discount Factor** To find the present value of future earnings of an employee, it has to be discounted at a particular rate.

The choice of rate can be as follows:

- Bank rate on loans (either prime rate or working gap rate)
- Companies return on capital employed

**Cost of Capital**

- Knowledge of individual human resource values could also affect employee bargaining power both within and outside the company.

- Publicizing human resource data could also have a disastrous impact on the attitudes of employees whose
resource value are declining. These employees may leave the organization or suffer loss of self esteem.

- Practical difficulty regarding HRA is quantification and pricing of employees in respect of jobs which do not yield any physical output.

  Determination of probabilities of the expected services of the employees is also a difficult task.

  These practical difficulties are subject to the influence of age, qualifications, previous experience, point of first entry, employment period and turnover as well as the organizational pulls and pressures on different categories of employees.

23. **Ethical & Behavioural Limitations** Human Resource Accounting is also viewed as a method of exercising autocratic control and manipulating employee behaviour. Human Resource measures promise to be powerful tools, and such manipulation would not only be a violation of management’s ethical responsibility, but it would almost certainly have a negative effect on organizational climate and individual attitude. Moreover, the behavioural problems associated with the gathering and reporting problems associated with the gathering and reporting of such data are extremely complex.

  Furthermore, people may react unfavorably as HRA attempts to attach quantitative values to them. Cultural constraints and taboos may create difficulty in arriving at accurate human resource value.

24. **Ownership Criterion** Traditionally, accountants insist on legal ownership and future benefits to be received to treat
certain cost an ‘assets’. Human Resource Investments have not been regarded as assets in the past as they are not similar to fixed assets. However, it can be argued that an organization should account for and monitor those resources which are most significant in the organization without regard for legal ownership or certainty of the value represented, and human resource meet such a criterion.

The costs or values associated with human resource should be capitalized and matched against future benefits accruing to the organization from such human resource.

25. Audit of HRA Information The reporting of HRA information in external annual reports brings with it the question of its audit. Costs incurred in human resource are readily subject to verification by the auditor and thus present no new problems.

Cost expirations, on the other hand if based on the theoretically sound assessment of future benefits remaining for the organizations, present some problems for the auditor because human resource and behavior are highly complex.

But, conventional accounting also uses estimates assumptions in many areas such as depreciation related to the future which could be as unpredictable and less accurate.

The verification of value-based data for human resource in annual reports presents a different and more substantial problem for the auditors.
6.2 PERSPECTIVES OF HRA IN INDIA

The following work can be taken up for further investigations:

1. The performance of an enterprise is very much dependent on the collective efforts of the management and the associated employees of the organization. As the directors are part and parcel of such enterprises, value of these people to the organization should also be represented in the balance sheet to make it perfect and more informative. Research in this section is warranted.

2. The findings show that there is a wide acceptance among executives and stakeholders of the usefulness of human resource values. Developing a suitable model for the purpose of computing the value leaves scope for further research in the area and this will hopefully throw greater insight into the scope for measuring and using human resource data by management.

3. The present study proves that human resource value depends upon number of variables; all these variables affect the value. At present in depth research on impact of different variable on human resource value is warranted. So, that proper valuation method can be developed and accurate value of human resources can be calculated and inter firm comparison can be done.

4. The different approaches/ models have been advocated by different proponents in the field of HRA. It is evident from the study that all these models have different backgrounds and different theoretical foundations.
Most of the public enterprises in India had adopted Lev & Schwartz Model for valuation of human resources. Since applications of Lev & Schwartz Model requires estimation of its various components may not be much helpful in the objective of the investigation. That is why enquiries to be made how the impact of subjectivity value of these services, discount factor and similar items can be minimized.

5. Analysis based on data of a single year has also some significance. But it would be important for inter-period comparison of performances of individual units. This will help to have an idea about the trend of the activities of public enterprises. Investigation in this direction is most desirable.

6. Inter-Unit comparison is very important for the enterprises. The shareholders, investors, creditors are usually confronted with the dilemma as to where they should allocate how much of their funds. Enquiries to this end will provide an idea on the effective use of resources bestowed to the individual units.

7. Even after the thirty three years of the commencement of HRA in India, a few public enterprises are disclosing human resource accounting information. In India, none of the regulatory authorities has issued proper guidelines for valuation and reporting of human resources and its accounting and this had created obstacle in the development of HRA practices in India. At this juncture serious and sincere research in this section is warranted.
8. HRA is useful to management in taking decisions regarding promotion, transfer, training, recruitment and retrenchment of employees. HRA is needed for better performance appraisal and manpower assessment: the management can also realize the present value of the future commitment for providing employee compensation. So, accurate data base of employees and their value is needed by top level management. More in depth research in needed in this direction.

9. The employees contribute and play a major role in the development of the organization. Human Resource Valuation helps in evaluating the expenditure incurred on training and development.

It ensures relative assessment of productivity, profitability and return on investment because of the fact that expenses are viewed from the investment perspective.

10. Motivation of employees is needed to increase their worth. It is most important to attract future employees and to retain present eminent and qualified workforce. HR value services as a benchmarking parameter with other value presenters of the industry. Further investigation in this area is needed.