

EMPLOYEES AS AN ASSET : A CONCEPTUAL DEBATE

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ABSTRACT

Conventional accountants treat expenses on employees as revenue expense which leads to affect the figure of profit or loss of that particular year. In the present paper it has been advocated that these expenses should be treated as capital expenditure or as asset which would help the organisation to have sound decision making mechanism. It is discussed in the paper that what are the qualifications to treat a particular head as asset. Five basic qualifications are analysed in detail keeping physical assets and human assets at one level. This paper is just one such effort, in the series of many, to convince accounting bodies to form one opinion about this neglected asset and make efforts to include its treatment in the existing Accounting Standards.

The existing accounting standards do not provide and recognize accounting for human resources, i.e. employees. Efforts are being made at national as well as international level to first form one opinion about recognizing human resource as most important and valuable asset and then to value them accordingly. In the present paper it is discussed whether employees fulfill the criteria of being asset. The accounting concepts have been compared while keeping physical assets and employees at one level. The accountants, researchers, economists, sociologists and management scientists have been talking about the important role played by the employees in an organisation. But at any stage their contribution has not been given the attention due to it.

Employees of an organisation have been viewed by the proponents from different angles, an asset, liability, deferred revenue expense or expense. But in the present paper it is advocated that they are the asset of an organisation.

Therefore proper disclosure of this effect should be made in the books of accounts. Thomas J Peters and Robert H Waterman Jr. (1) have talked about human resource in their book, 'In search of Excellence'. According to them, "*If you want productivity and the financial reward that goes with it, you must treat your workers as the most important asset.*" The proponents of Human Resource Accounting (HRA) - Hermanson, Heikiman and Jones, Likert, Flamholtz and Pyle, Woodruff Jr., Lev and Schwartz, Elias, Caplen and Landekich, Dermer and Siegel, Hendricks, J R Dyson, Linda Lewis etc. have accepted and recognised human resource as an asset and even they have suggested different models of valuing human resource.

Employees become an organisational asset by their potential capabilities. The organisation acquires the individuals who together work for the attainment of organisational objects. Employees are recruited through screening and different selection procedures in a way same as physical assets are acquired.

They are provided training, on-the-job or off-the-job, to perform their best for the organisation. Whatever services are desired by the Organisation, employees are utilised for that. Different strategies of performance appraisal and job evaluation are also followed to get best result out of the human resource. Just like physical assets, employees are equipped with training and development schemes to cope with the latest technology in the market. It maintains or increases the worth of their capacities.

Likert (2) is of the view that the activation level and the resultant performance level achieved on the assigned tasks by the individuals could be governed by the joint interaction of the extent of matching between the assigned job requirement factors and the individual's traits and attributes, forces in the complex system of which the individual is a member, various policies of management pertaining to compensation, promotion, reward and welfare measures, organisational characteristics like leadership style, level of participation, nature and extent of communication, mutual trust and confidence. In his research he concludes that human productivity would have high correlation with the level of satisfaction received by the individuals, which would in turn depend on the extent of the fulfillment of individuals' various needs and aspirations.

If it is his finding then, why is it that the satisfaction of an employee in an organisation is not valued? The satisfaction will depend on fulfilment of his needs and proper rewards for his work. Physical assets as compared to employees at no level or at very low level change its needs and values with the age of

organisation. Human beings are ever evolving productivity factor (3). They can develop themselves to attain latest capabilities and higher level of competency. The individuals in an organisation needs continuous psychic care (4) to retain them as an effective member of the human organisation. This important feature of human resource is very distinct from physical assets. Physical asset do not have their own mind to be retained in an organisation. That is why their valuation becomes very easy. But does it reflect the clear financial position of an organisation? There may be some contradiction about valuation of intangible assets. The value of stock-in-trade changes according to the market situation. If these flexibilities are allowed then what is wrong in giving worth to employees or treating them as an asset?

So far as conventional way of accounting treatment is concerned employees are not treated as an asset and therefore not reflected in financial statement(5). The employees are treated as revenue expenditure like material, stationary or carriage. How can one expect that financial statement is reflecting clear financial position of an organisation if the cost incurred on individual employees for recruitment, training and development etc. are mostly combined with general overhead charges of the organisation? There is no mention of loyalty of customers, suppliers, share holders and firm's reputation in the community, in balance sheet. Is it just enough to show goodwill which, according to traditional accountants include all such values?

If conventional accountants will continue to show cost of employees as an expenditure, the amount of profit would

not be justified. One hundred percent depreciation of employees in the very first year leads to postponement of profit recognition and tax payment (6). This is how the most important asset, the loyalty and ability of employees is neglected. So far as true and fair figure of profit is concerned it would never be there if the expenses incurred on recruitment, training and development etc., and any investment towards employees will be treated as an expense. Employees appointed today will not leave the organisation tomorrow. Amount paid for their training will repay it in the way of quantitative and qualitative production in the years to come. To increase the amount of profit the organisation may think of avoiding training and development expenditure, which will result negatively. Investment on employees may also be avoided by the organisation in view of showing more profits. This will also disturb profitability. The incomes would keep on being understated, and expenses overstated. Such decisions of management would provide short term gains at the cost of long term losses. Management may even be engaged in such actions as to decrease the quality of human resources to enhance the present level of profits.

It is true that the management will be interested in maximum profit at minimum cost. But how far is it good at the cost of avoidance of expenditure on human resources? Just because it does not provide short term gain! There is a very simple way out here which is to treat expenditure on employees as a capital expenditure - treat employees as an asset. This will in one way help management to show fair profit. On the other hand it will

motivate workers to work more qualitatively and efficiently.

One more very important aspect is avoided by conventional accountants which is investment on human resources. While calculating return on investment employees are never taken into account which should be. Without including employees investment in the capital employed, the return on investment would not be proper, true and fair. Return on investment guides management to take effective and sound decisions. It helps in framing future policies. Therefore if this will not be proper, almost all important policies will be affected. According to Sadan and Auerbach (7), *'such omissions to account for human resource (employees) are causing uneasiness inside and outside the accounting profession.'* Whenever transparency in accounts is talked about this aspect of employees should not be neglected.

Now let us come to the definition of an Asset and test whether employees qualify to be included in it. As early as in 1929 John Canning started searching for the correct definition of asset and interestingly he concluded that not all items with the characteristics of assets are commonly included on the Balance Sheet and that some items that do appear are not really assets(8). Such was the case in 1929, one can even reach this conclusion today as employees are still not being considered as assets so far as Accounting Standards are concerned. Hermanson took the liberty of defining assets as :

Assets are scarce resource (defined as services but grouped by and referred to as agents), operating within the entity, capable of being transferred by forces in the economy, and expressible in terms of money;

which have been acquired as a result of some current or past transaction and which have the apparent liability to render 'future economic benefit. (9).

This definition includes certain types of assets also which is not followed by conventional accountants.

In the above study it is pointed out that one thing is sure about employees that they should not be treated as an expense item. It is also highlighted here and elsewhere, that it is an asset and should be treated accordingly. For qualifying as an asset it should :

- be owned by an organisation,
- be measurable,
- render future economic benefit,
- be transferable, and
- be acquired through a transaction.

Building, Plant, Land or Machinery - all such physical assets are owned by organisation, are available for being transferred, are measurable, have future economic benefits and of course, are acquired by a transaction - that is why they are assets shown in the Balance Sheet. Investment also qualify this criterion. Now let us test employees, whether they qualify for being treated as asset. We can talk about it taking into consideration each qualification one by one.

1. Whether employees are owned by an organisation or not. Basically there are two types of ownership - Legal and Operational. So far as employees are concerned they cannot be owned, but the services provided by them can very well be owned. Like other physical assets when an individual is appointed, he becomes an employee. His name starts appearing in the attendance register, his name is added in the list of employees when he joins the

organisation, now his services are owned by the organisation. As a person he is not owned, but as an employee his services are owned. American Accounting Association (10), recommended that accounting is primarily concerned with events and objects that have economic significance and it does not necessarily involve legal ownership.

So far as operational ownership is concerned, as regards employees it applies clearly as their services are owned. Highly trained sales force is an example of operational asset, it is not directly usable or convertible for the payment of entity debts (Hermanson). There may be operational negative assets which will include the factors relatively inefficient and untrained sales force. Therefore the services, capacities, skills and experiences which results into qualitative production, are an asset.

2. Whether the worth of employees is measurable or not. It is of course a difficult but not an impossible task. There are quite a lot of models proposed by different researchers. These models are based on basic accounting concepts and doctrines. These models are being followed by different organisations in different countries depending on the accounting and social environments. Most of the proposed approaches, being subjective in valuing employees, objective criteria of conventional accounting practices posed a problem for gaining acceptance amongst the accountants. American Accounting Association has also accepted this practice subject to development of appropriate means of measuring the same in its committee report on HRA.

So far as Indian Companies are concerned there are some 12-15 private

and public companies - which have started valuing their employees. Some of them are BHEL, EIL, Maruti, SAIL, ONGC, NTPC, CCI, SPIC ACC, HSL etc.. Though in their annual accounts they show Human assets, such disclosure is not audited in the absence of an Accounting Standard.

Maruti experience is very favourable and motivates employees to perform their best. *At Maruti, the proposal is to employ about 4000 employees at peak production volume of 100000 vehicles per year. This productivity target of 25 vehicles per employee is 10 times the existing norm in Indian auto companies and 2.5 times the European norm. Through this measure it is estimated that Maruti's labour cost would work out to only Rs.1200 per vehicle* (11). This is because of the importance given to its employees. Therefore it is not a problem to measure the value of employees any more.

3. Whether employees render future economic benefit or not. The expenses incurred on recruitment, training and development carry future economic benefits as an employee is recruited once in the life of an organisation. Training given to them is not going to help just for one year. It will help in the whole life of the organisation. Here it should also be admitted that even the salary given to an employee carries future economic benefits with it because it decides the stay of an employee. Therefore, it carries future economic benefits and qualifies for being treated as an asset. The increments, facilities, working atmosphere, good employer-employee relation, good career growth, all these factors make an employee work in an organisation with full

sense of attachment. The expenses incurred on improving working conditions, creating good atmosphere or on any head which decides the stay of an employee should be treated as an asset the reason being, it carries future economic benefits. Future economic benefit being the main characteristic of an asset, American Accounting Association has advocated that human resources may be considered as assets as they involve an element of future usefulness. *'The expenditure on employees need to be analysed, expenditures pertaining to future benefits may be considered as assets and pertaining to current benefits as expenses'* (12).

There are very interesting facts about expenditure on training and development. Training can be classified in two categories - general and specific. The organisations provide training according to their need. If general training is given to an employee this training involves future economic benefits both to the employee as well as to the employer. If employees are trained but not rewarded accordingly, they may prefer to skip to another organisation because there will be an increase in the market value of such employee. On the other hand if specific training is provided, the probability of skipping to another organisation would be less. The expenditure incurred increases the value of asset. Before providing training to employees, the organisation should ensure that training is effective and there are conditions under which the employee would not skip to another organisation. Such asset creation may also be claimed by an organisation if an employee leaves the job depending on the terms and conditions of providing training to him.

Thus training may not necessarily lead to creation of human assets even if it is presumed that it would be effective in work situations to improve productivity. It 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 (13). So now it is clear that expenses incurred on employees involves future economic benefit.

4. Whether employees are transferable or not. It is true that employees cannot be sold. But their services can be sold. The fundamental principle of ownership of employees is related to the services provided by employees. An employee may choose to leave the organisation but a physical asset cannot. An organisation can be sold or transferred to another organisation with its employees depending on the consent of its employees. The question of consent does not arise in case of a physical asset. This consent is the most important part as far as transferability is concerned. The consent is formed by looking at the management of an organisation. Therefore there can be transfer of services of the employees.

5. Whether employees are acquired through transaction or not. When an individual is recruited he or she agrees to accept an amount as salary. Traditionally speaking, recruitment does not give birth to a transaction. But is it correct? There are certain terms and conditions of employment which have to be followed by employer as well as the employee. When a person is appointed, a transaction takes place and when he or she starts working with the organisation the agreed amount of salary or wages becomes due. The

expenses incurred on interview, screening or induction can very well be treated as a capital expenditure. One very important aspect is that the employees are not acquired for disposal but for continued services in the organisation. The commitment to pay salary to an employee in itself is not a transaction but the moment employee joins the organisation and starts working it becomes a transaction.

Thus, it is evident that the criteria of being an asset is fulfilled by employees and their services in an organisation. Employees are none the less an important asset than any physical asset. With the changes in the development of management and industries it is needed to make a shift from conventional way of accounting. If an advertisement can appear on television like - we make people, we also make steel - why employees are not getting place in the Balance Sheet. In the President's or Chairman's speech of an organisation it is always being mentioned that without the active role of employees it would not have been possible to have such amount as profits. Why is the active role of employees not disclosed in the Balance Sheet?

The idea of treating employees as an asset is not aimed at lowering the status of human dignity. The future socio-economic systems will be dominated by the challenges of change in the industrial environment to enhance the productivity of all kinds of resources. Human resource would occupy an imperial status with the predominance of increasing social complexity. (14).

It can be concluded here that the employees should be treated as an asset since they qualify the test of being an asset. There may be lot of other aspects which may be involved in the treatment of

employees as an asset. An attempt has been made to convince the accounting fraternity to treat employees as an asset so far as financial disclosure is concerned. The accounting bodies should decide that whether treating employees as an asset would result positively or negatively. Such treatment will help the management to have sound decision policy. On the other hand it would motivate employees to perform their best. It would also develop a sense of attachment towards the organisation. The employees would come to know their own organisational value, correspondingly and would be encouraged to achieve the organisational goal.

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