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Human Resource Accounting: The Missing Element in the Statement of Financial Position. Empirical Evidence from Ghana

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Abstract
The human resource is the most valuable asset of any business organization. This is because it utilizes other resources to create value for the organization yet it is not incorporated into the statement of financial position of the business. This paper examines what accounts for its exclusion and the way forward. A descriptive research design was deployed for the study. A purposive sampling method was used to select 140 members from the Institute of Chartered Accountants (Ghana) with a response rate of 82.1%. It was revealed that the inclusion of the human resource in the Statement of Financial Statement cannot be achieved now until broader consultation and participation of key actors in the accounting field. The key challenges include initial and subsequent measurement problem; distortion of shareholders' networth; there is no standard or law that supports its inclusion and lack of active market for human resource. Developing an appropriate and acceptable model for Human Resource Accounting is very difficult to achieve because of the variables to include in the model. The paper, however, recommends that the International Accounting Standard Board (IASB) should engage key actors and experts in the accounting field to debate on the pros and cons of human resource inclusion in the Statement of Financial Position.
Keywords: Human Resource; Statement of Financial Position; Model; Standards; Value; Measurement; Assets

1. Introduction

The users of financial accounting information are interested in the correctness, completeness and accuracy of financial statements so as to make informed decisions. To achieve this, IAS 1 which deals with Presentation of Financial Statements, outlined the financial statements to be presented to users. These include:

i. Statement of financial position
ii. Statement of profit or loss and other comprehensive income
iii. Statement of changes in equity
iv. Statement of cash flows
v. Notes to the accounts
vi. Comparatives

The components of these financial statements include Expenses, Revenue, Assets, Liabilities and Equity. This paper focuses on the assets components. International Accounting Standard Board Conceptual Framework (2015) described an asset as a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the enterprise. By this definition, human resource is covered adequately but it is the element that is missing in the Statement of Financial Position. According to the American Accounting Association (1973), Human Resources Accounting is the process of identifying and measuring data about human resources and communicating this information to interested parties. Micah, Ofurum and Ihendinihu (2012) viewed human resource (HR) as people's energies, skills, talents and knowledge, which are, or which potentially can be applied to the production of goods or rendering useful services. Human resource accounting deals with valuation of the contribution of human resource to organizational performance and reporting it in the financial statements for the purpose of decision making and planning by the stakeholders.

The general view is that, among all the assets of an organization, human resource is the most valuable assets (Oseni & Igbinosa, 2015; Roseline & Kayode, 2015). This is because they make decisions and utilize the other assets to create value for the organization and yet it is not incorporated into the statement of financial position of the business. Hossain, Khan and Yasmim (2004) attributed this to difficulties in measuring experience, knowledge, skills in accounting terms. The only accounting treatment for human resources is to recognize all associated cost as period cost and therefore, missing in the statement of financial position. This treatment suggests that the service that human resource provides is consumed within one financial year and does not have any future effect on the performance of the company. However, this is not the case in the sense that every organization has a long-term strategic plan and this is a product of human resource. Obara (2013) suggested that firms should exclude human resource value from Profit and Loss Account and then include it on the balance sheet. The growth and survival of an organization depend largely on human resources (Raunak, 2010; Brian, Thomas & Matthew, 2014; Kalpana, 2016; Onyinyechi1 & Ihendinihu, 2017 and Vitalii, Nataliia, & Mariya, 2017). It can, therefore, be argued that the benefits derive from human resources is not only for short term but long term too.

There have been many attempts in the past and recent years by scholars and experts to develop models appropriate for human resources to be included in the financial statements (Scoth, 1925; Hekimain & Curtis, 1967; Likert, 1967; Lev & Schwartz, 1971; Flamholtz, 1973; Dobija, 1998; Flamholtz, Bulen & Hua, 2002 ; Tollington & El‐Tawy, 2010 and Arkan, 2016) and still up to date, it appears that firms are not willing to incorporate human resource into their financial statements. Osemeke (2017) pointed out that most of the models did not provide how a human resource should be recorded and disclosed in the financial statement. The standard setters are reluctant to issue a standard on human resource accounting making it a requirement for the presentation of financial statements. The work of Passard, Kaitlin and Vyas (2012) revealed that 87% of the respondents were not in support of human resource inclusion in the balance sheet. This suggests that there are more factors hindering Accounting for Human Resources in the financial statements and not just models for valuations. As Mustafizur, Amzad and Tabassum (2013) put it, most of the existing models are not even acceptable worldwide. Therefore, this paper specifically looks at the factors hindering accounting for human resources beyond valuations.

2. Literature Review

2.0 Introduction

This section covers some proposed models for human resource valuation, Effects of Human Resource Accounting on the financial statement, the reasons for excluding human resource from the Statement of Financial Position.
Importance of Human Resource

2.1 Valuation Models.

The first stage in human resource accounting is to develop appropriate models that will ensure true and fair presentation of human resource in the financial statements. If the right models are not developed, any attempt to include the human resource in the financial statements will mislead users. Empirical Literature covered many models for human resource accounting including Lev and Schwartz Model (1971), Stochastic Model of Eric Flamholtz (1972), Morse Model (1973), Lev and Friedman Model (1974), Hermanson Model (1964), Ogan Model (1976), Hekimian , Jones Model, Likert Model (1967), Boudreau Model (1998) and Dobija Model (1998) as cited in Andrade and Sotomayor (2011). Afolabi (2014), however, classified the proposed models into Historical Cost Models and Value Approach Model.

With the Historical Cost Model, the components for human resource valuation are recruiting; acquisition; formal training and familiarization, informal training, informal familiarization; experience, and development. The leading proponents of this model were Brummet, Flamholtz and Pyle (1968). The main argument for this model is that the cost associated with the human resource should be capitalized and reported in the statement of financial position. The portion of human resource consumed within the financial year should be determined and reported in the Income Statement by using amortization system. However, the issue of amortization of human resource is perceived to be a challenge to accountants because of uncertainties (Arkan, 2016).

As cited in Oluwatoyin (2014), the Value Approach Model was championed by Lev and Schwartz (1971) and they argued that the future value of a human resource can be discounted in present terms and then report in the financial statement. Under this model, human resource is valued using the following formula:

$$\sum(Vy) = \sum Py\,(t + 1) \sum I(T)\,(1 + R)^{t-y}$$

Where: $\sum(Vy)$= expected value of a 'y' year old person's human capital
T = the person's retirement age
Py(t) = probability of the person leaving the organization
I(t) = expected earnings of the person in a period
Ir = discount rate.

One major weakness of this model is that most of the variables considered are based on estimation and once labour environment cannot be predicted with certainty, the estimated variables may not reflect the true situation. This can lead to overstating or understating human resource value in the financial statements. In the view of this, Haddad (2014) argued that a key obstacle to human resource accounting is lack of reliability in the measurement of Human Resource. Another issue with this model is that it failed to include knowledge, experience, skills and contribution of human resource. These variables are key in human resource valuation (Hossain, Khan & Yasmim (2004). In line with this, Kenneth and Srinivas (2004) opined that people with high skills have higher human capital value than those with lower skills. They further posited that young people have greater value than older people because the young person has a longer expected work life holding other factors constant. Tollington and El‐Tawy (2010) argued that the emphasis should be placed on the output that is what human resource create rather than input orientation. This suggests any model that did not consider human resource output would not fairly give the right value of the human resource.

2.2 Relation between Human Resource and Firm's Performance

The success of every organization depends on the quality of human resource it has (Weatherly, 2003). Empirical evidence suggests that human resources have positive and quality effects on firm's and country 's performance (Vipin, 2015). Akintoye (2012) carried out a research work using Lev and Schwartz (1971) Model on Oceanic Bank Plc and the result revealed that there was a positive relationship between human resource and profitability of the business. The study of Ishola, Olowolaju and Odewusi (2015) corroborated the findings of Akintoye (2012)**.** The work of Gustavo, Luiz, Umbelina, and Joao (2016) indicates that there is a positive correlation between human resources disclosure and firm's performance among listed companies in Nigeria. These studies support the assertion that human resources are the most valuable assets of a company and therefore, special attention should be given to it by management in terms of recruiting the right people, providing the best working environment, good condition of work and training and development.

2.3 Challenges in dealing with Human Accounting

As Cited in Arkan (2016), Gates (2002) and Akinsoyinu (1992) were not in support of including the human resource in the financial statements. The reasons they advanced include but not limited to:

i. human resource is a sensitive data of an organization and cannot be shared externally.
ii. measurement not a first priority for the company. This is because companies are interested in how to utilize the human resource to improve performance and not measurement.
iii. not enough time and resources
iv. human resource professionals unaware of value or no clear return on investment.
v. The standard setters and other regulatory bodies did not cover it to make it a requirement for the purpose of international financial reporting
vi. Global and group issues. Different countries have different labour laws meaning that human resources are treated differently in terms of job valuation, job placement, remuneration and retirement plans. This means that harmonization of international accounting standards would create a problem.

Kenneth and Srinivas (2004) classified human resource as a contingent asset and the challenge of this asset is that it cannot be fully liquidated in a short period because there is no active market where one can transfer his skills for a fee. Another challenge is measurement problem (Haddad, 2014)

Other researchers were of the opinion that including human resource in the financial statements would dehumanize people and treat them like machines. It will also distort the measurement of return on investment (Alnasser, Shaban & Atieh (2014). Oseni and Igbinosa (2015) suggest that if even human resource is to be included in the financial statement, it should be a separate human capital report that would provide statistics and other facts about a company's stock of human capital. A company has no full control over human resource because their services are hired and not purchased and the worker can leave the company at his will. A balance sheet of a company that experiences high labour turn over would be unstable if human resource is reported as an asset and this has decision implications.

2.4 Effect of Human Resource Accounting on Net worth of Shareholders

It is important to consider the effect of human resource inclusion in the balance sheet on the net worth of shareholders. Net worth is defined as total assets less total liabilities. This indicates the assets that can be distributed to the shareholders in case of liquidation or capital withdrawal. While others assets can be sold, human resource cannot be sold meaning the shareholders would lose human resource portion of the net worth. Kenneth and Srinivas (2004) were of the view that human resource cannot be exchanged for fee due to lack of active market. Haddad (2014) observed that treating human resource as asset by capitalizing the investment motivates them to work hard and this has the potential of increasing shareholders' fund and creating favourable image for the company. However, once human resource is capitalized, it forms part of net assets. Even though the owner has the right to dispose of human resource just like the other assets when the need arises, it comes as a cost in the form of compensation instead of receiving value for it. Therefore, when human resource is disposed of, it brings no value to the shareholders. This means that capitalizing and reporting human resource in the statement of financial position inflates the net worth of shareholders.

3. Methodology

The Study used descriptive research approach as there was no plan to manipulate any variable but to explain existing phenomenon. The population consists of only members from the Institute of Chartered Accountants (Ghana). A sample size of 140 was used through purposive sampling. However, only 115 questionnaires were retrieved and analysed making a response rate of 82.1%. The participants were reached through email and personal visit. SPSS software was used to process the data for analysis and discussions.

4. Results and Discussion

This section deals with analysis and discussion of data obtained from the participants.

Inclusion of Human Resource in the Statement of Financial Position

This study solicited the views of the participants on the inclusion of Human Resource in the Statement of Financial Position. A question was asked as to whether they support the school of thought that Human Resource should be measured and reported in the Financial Statement or not. Figure 1 depicts the results.

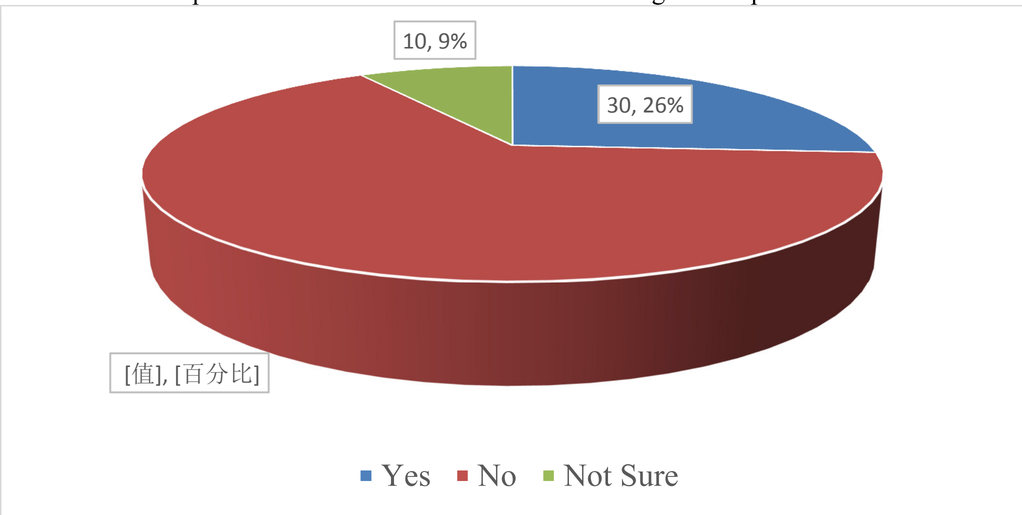

Figure 1: Reporting Human Resource in Financial Statement

Empirical evidence from Figure 1 suggests that the respondents had mix reaction as to whether Human Resource should be included in the Statement of Financial Position or not. The majority (75) representing 65% of the participants were of the view that human resource should not be reported in Statement of Financial Position. Others (30) representing 26% of them think human resource as valuable as it is should be reported in the financial statement while 9% took a neutral position because they were not sure as to whether it should be included or not. This confirmed the work of Passard, Kaitlin and Vyas (2012) who indicated that human resource should not be accounted for and reported on the balance sheet.

The arguments advanced by those who were not in support of it include the following:

i. There is no appropriate model for measurement of human resource which leads to subjective measurement. This defeats the uniformity concept which is one of the qualitative characteristics of financial statement and comparability becomes a problem.

ii. They were also of the view that, the reward of labour is wages and salaries and once it is treated in Income Statement, there is no need to include it in the Statement of Financial Position.

iii. Human Resource is a key aspect of the firm's competitive intelligence and the inclusion of it would expose the firm to its competitors.

iv. It is a sensitive data of the organization

v. It would not be in the interest of shareholders because they receive nothing if not incurring additional cost if human resource is disposed of.

However, the participants who supported the idea of including the human resource in the Statement of Financial Position indicated that human resource is a key asset of every organization and therefore, should be included. They further stressed that the benefits associated with human resource flow to the entity over a reasonable period of time and are not exhausted within one financial year and therefore, should be included in the Statement of Financial Position.

Role of Standard Setters in Human Resource Accounting

The International Accounting Standard Board (IASB) has the responsibility of issuing, revising and reconciling Accounting standards. In line with this, the participants were asked whether they agree that IASB should revise the standards to cover Human Resource and make it a requirement for corporate organizations to include it in financial reporting. Table 1 below presents the views of the respondents.

Table 1: Role of Standard Setters in Human Resource Accounting

Response	Frequency	Percent
Yes	83	72.2
No	17	14.8
Not Sure	15	13.0
Total	115	100.0

The majority (83) representing 72.2% of the participants agreed that IASB should revise the standards to cover Human Resource. However, 17 representing 14.8% disagreed while 15 representing 13% decided to remain neutral. The majority of the participants think that, if Human Resource is to be included in the Statement of Financial Position, then IASB should revise the current standards to cover Human Resource Accounting. They proposed a common valuation model should be developed to avoid subjective measurement and the variables of the model should include the following:

i. Knowledge, Skills and Experience
ii. Contribution or output
iii. Age
iv. Qualification, grade and field of expertise
v. Basic Salary
vi. Continue Professional Development cost and other cost
vii. Estimated Rate of turnover
viii. Years of service
ix. Discount rate
x. Insurance and pension cost

It can be concluded on the basis of these variables that, developing an appropriate model for Human Resource Accounting is very difficult. Some of these variables cannot be determined with certainty. Any model develops from these variables would be subject to manipulation by management.

Challenges Associated with Human Resource Accounting

The study examines the challenges associated with Human Resource Accounting. The challenges were presented in the form of Likert-type of scale and the participants were to provide their answer using Strongly Agree (SA), Agree (A), Undecided (U), Disagree (D) and Strongly Disagree (SD). See Table 2 for the detail results.

Table 2: Challenges Associated with Human Resource Accounting

Problems of Human Resource Accounting	SA/A		U		D/SD	
	No.	%	No.	%	No.	%
Initial and the subsequent measurement problem	115	100%	0	0	0	0
It is not required by any standard or law to be included	115	100%	0	0	0	0
It does not involve in arm-length transactions (No active market for the human resource)	100	87.0%	0	0	15	13%
The contribution of individual workers to the firm's performance cannot easily be determined like any other assets	100	87%	15	13.0%	0	0
Financial Position of the business may be misleading when included	80	69.6%	20	17.4%	15	13%
Valuation problem in case of merger and acquisition	81	70.4%	34	29.6%	0	0
Distortion of shareholders wealth	84	73.1%	15	13%	16	13.9%

Note: SA/A=strongly agree/agree; U=undecided; D/SD=disagree/strongly disagree

Statistical evidence from Table 2 revealed that all the participants (115) agreed that initial and subsequent measurement would be a major challenge in Human Resource Accounting. With regard to Property, Plant and Equipment (PPE), IAS 16 provides that a tangible non-current asset should initially be measured at its cost and subsequently be measured using Cost Model or Revaluation Model but it is not clear how Human Resource should be initially and subsequently measured. The participants pointed out that, this challenge would create room for subjective measurement. Another challenge all the participants agreed with was the issue of standard and other laws. At present, there is no standard or legal requirement for its inclusion in the Statement of Financial Position. The majority (100) representing 87% of the participants agreed that there is no active market for the human resource while 15(13%) disagreed. Transactions regarding human resource do not involve in an arm-length transaction. This means that fair value of human resource would be difficult to determine.

It was also observed that the contribution of individual workers to the firm's performance cannot easily be determined like any other assets as 87% of the participants agreed with it. As few as 15 (13%) were not able to give their opinion on it. As suggested by the respondents, the contribution or output of the human resource should be part of the model. So if the contribution cannot easily be determined, then the model cannot fairly value human resource. This creates room for subjective valuation of human resource leading to discrimination among workers in respect of their value. When this happens, there is a tendency of underperformance because others would be dissatisfied because of the value management placed on them. It is also difficult to compare performance of similar companies if human resource is measured subjectively.

On the issue of distortion of shareholders' wealth, 73.1% of the participant agreed that the inclusion of the human resource in the financial statement would distort their wealth while 13.9% disagreed and 13% remained neutral. This is true because the shareholders cannot receive human resource as a return. It would not be in the interest of shareholders for the management to include the human resource in the financial statement as it is not part of their value. Valuation in case of merger and acquisition was also identified as a challenge as 70.4%

agreed with it. It was also revealed that the statement of financial position of the business may be misrepresented and this was supported by 69.6% of the participants. However, 13% did not think it would lead to misrepresentation of the financial statements while 17.4% decided to remain neutral.

Conclusion and Recommendation

On the basis of the findings, the following conclusions can be drawn:

i. The inclusion of Human Resource in the Statement of Financial Statement cannot be achieved now until broader consultation and participation of key actors in the accounting field.

ii. Developing an appropriate and acceptable model for Human Resource Accounting is very difficult to achieve because of the variables to include in the model.

iii. The shareholders would not welcome the idea of capturing human resource in the financial statement as it distorts their value.

iv. Human Resource is a key aspect of the firm's competitive intelligence and a rare asset and therefore, it must be protected. The inclusion of it in the statement of financial position would expose the firm to its competitors.

v. The current human resource models need improvement to include certain key variables to make them acceptable internationally.

vi. The inability to measure the contribution of human resource to firm's performance fairly, creates room for subjective valuation of human resource leading to discrimination among workers in respect of their value and difficulties in comparing performance of similar companies.

vii. Human Resource Accounting can be adopted by firms if standard setters and regulatory bodies such Stock Exchange Commission, Tax Authorities, Registrar of Companies support its inclusion. No single firm can adopt it without legal backing.

The Paper recommends that the International Accounting Standard Board (IASB) should engage key actors and experts in the accounting field to debate on the pros and cons of human resource inclusion in the Statement of Financial Position. This will provide the board with the next line of action to take in respect of Human Resource Accounting.

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