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HUMAN CAPITAL ACCOUNTING: THE DICHOTOMY OF VALUE REPRESENTATION

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Abstract

The study is an attempt to examine the weakness in the current method of reporting and treating the human capital value within the firm reporting system. A survey method was adopted using structured questionnaire the chi-square a non-parametric method of data analysis with used for the interpretation and data analysis. The study revealed that capitalizing the value of human capital using the discounted usage system means accepted as obviously better than the current realization method. It was recommended that productivity rather than only training and qualification should be used for promotion and value determination.

Introduction

Capital human remain the most valuation factor is the work organization, the process of securing, training and rewarding human capital however remain difficulty and cumbersome also being an asset of the organization means the value should be accounted for in the balance sheet of the firm, however, they are not machinery, property, land, buildings are all regarded as asset side of the balance sheet, in fact cash, debtor, etc are regarded as current asset of the firm and are accorded treated in the asset side of the balance sheet. However, the human capital value of a firm although are regarded as asset but are treated to the profit and loss account of the organization as an expenses. This pose a problem to the value accorded human capital as asset of the firm. Thus basic problem of human capital have made many organization today to invest less on human capital development other organization that doe invest on human capital do so is a selective manner. The other issue regarding human capital is the fluidity of human capital asset itself. It can die and go to extinction, or become obsolete, or leave the organization after huge investment on their development for other better opportunity this, thus limit the reliability of human capital unlike other asset of the organization. The asset difficulty regarding human capital have made their asset status in organization rather debatable not withstanding human capital remain the most value factor in the organization system for the obvious reason that human capital is the only factor that can effectively put all other factor to work. Thus, the problem arise of how to treat human capital value to the financial report of the organization should human capital value be treated as a pure asset of the firm or realized is the profit and cost account of the firm. The study therefore is an attempt to examine the current treatment is goal of estimating weather the current treatment is good enough or recommend other method for treating human capital value in the financial report of the firm therefore accorded better value in real term to human capital of the firm in boosting the market value of the firm.

Literature Review

Flamholz (1972) define human capital accounting as "The process of identifying, measuring and communicating information about human resources to decision makers Dess and Picken (1999) also define human capital accounting as "capabilities, knowledge, skills and experience of the company's employees and managers as well as the capacity to add to this reservoir of knowledge, skills, and experience through individual learning."

CEDEFOP (1998) define human resource accounting as the process of identifying, measuring and communicating information about human resources in order to facilitate effective management within an organization. It is an extension of the accounting principles of matching costs and revenues and of organizing data to communicate relevant information in financial terms.Human Resource Accounting is a technique of measuring the effectiveness of personnel management activities and the use of people in an organization. There are two approaches to human resource accounting, namely the cost approach, also called human resource cost accounting method or model and the value approach method, the cost approach include a) Acquisition cost model and b) replacement cost model. The value approach includes the present value of future earnings method, the discounted future wage model, and competitive bidding model, (Wikipedia). These definitions fails to recognize or give collective value to human capital, it also fails to account for the accounting estimation of the value of the human capital however, the definition is of import in capturing the need for determination of human capital value as an assets of the firm rather than treating it as an expenses.

Human capital theories

Economists estimate human capital on the basis of years of schooling or formal educational attainment levels regardless of actual productive capacity however, financial accounting and reporting leave human capital off the balance sheet for want of rules or conventions. Financial accountants and educators are developing methods for systematically evaluating and recording knowledge assets acquired through experience, education and training such that human capital accounting measurement become an issue in financial reporting ( ) Approaches to Human resource accounting was first developed 1691 the next stage was during 1691-1960 and third phase post-1960..(Wikipedia)

Determination of the value of a firm as been the bone of contention for financial managers, the "value" of an enterprise as measured within traditional balance sheets, include stating wasting assets such as buildings, production plant as fixed assets and others such as cash and stocks as current assets the two making the total value of the firm, while human capital value is regarded as expenses in measuring the enterprise's assets. However, with the growing emergence of the knowledge economy, this traditional valuation has been called into question due to the recognition that human capital is an increasingly important part of an enterprise's total value. This has led to two important questions: how to assess the value of human capital in addition to an enterprise's tangible assets and how to improve the development of human capital in enterprises. The emergence of methods for accounting for human resources aimed at measuring, developing and managing the human capital in an enterprise, can thus be said to reflect the need for improving value measurement and accounting for human capital value as well as ensuring effective human resource management. (CEDEFOP, 1998)

Flamholz (1973) was one of the earliest theorists to give serious thought to the problems of measuring the value of an individual. He argued that this should be based on three variables: productivity, transferability, and promotability (these could perhaps be seen as surrogate ways of measuring skills and knowledge). He also proposed, however, that the value of an individual will be linked to the likelihood that that individual will stay with the organisation (loyalty, perhaps measured by job satisfaction). The difficulty, of course, is measurement. It is possible to construct profiles of employees, assessed on key variables, such as loyalty, trust, motivation, effectiveness, experience, etc. Cataloguing these, individually, and in total, may give a useful insight into the development of the organisation. It could be, for example, that a short-term increase in profit has been brought about only at the expense of an overall decline in motivation

Flamholmay tz and Pyle (1985) developed the acquisition cost model. This method measures the organization's investment in employees using five parameters which includes recruiting, acquisition; formal training and familiarization; informal training, Informal familiarization; experience and development. This model suggest instead of charging the costs relating to human capital to profit and loss accounting it should be capitalized in the balance sheet. The process of giving a status of asset to the expenditure item is called capitalization; the capitalized value of human resource is thereafter amortized over a period of time. It is done by taking the age of the employee at the time of recruitment and at the time of retirement, out of these a few employees may leave the organization before attaining the superannuation; this value is aggregated and then amortized over the years. The limitation of this method includes false assumption that the currency value is stable. Secondly since the assets cannot be sold there is no independent check of valuation. Lastly, this method measures only the costs to the organization but ignores completely any measure of the value of the employee to the organization (Cascio, 1991).

Hekimian and Jones in Cascio (1991) proposed in relation to the value of human capital to the origination that where an organization had several divisions seeking the same employee, the employee should be allocated to the highest bidder and the bid price incorporated into that division's investment base. For example a value of a professional athlete's service is often determined by how much money a particular team, acting in an open competitive market is willing to pay him or her.

OECD (1996) in relating the concept of human capital accounting to "return-on-investment" (ROI) in education and training, and education/training reform, the OECD notes that it is common practice in most countries for industries and firms to make budgetary decisions on funding for compulsory schooling based on the assumption that the social and economic benefits outweigh the costs; however, in many areas, the requirements of the knowledge-based economy increase the pressure to improve the effectiveness and efficiency of human capital formulation. It is concluded that "a variety of problems are posed by the predominant methods for assessing human capital that are geared to the needs of an education system that extracts fees by controlling credentials as opposed to a system where the output potential of human capital is measured on the basis of competence to produce regardless of how much knowledge was acquired." However, one of the obstacles to measuring the output potential of human capital is the segmented and oligopolistic character of educational and professional certificate which is based on the historical power of universities and professions to forbid the utilization of acquired competences without certificate which is a measure of how well individual have acquire professional and academic knowledge. The traditional state-sanctioned assertion of property rights over the knowledge acquired when people invest in human capital is one way of resolving the paradox of knowledge as a public good and as inalienable (OCED, 1996)

The accounting of human resources can be seen as just as much a question of philosophy as of technique. This is one of the reasons behind the variety of approaches and is further underlined by the broad range of purposes for which accounting human resources can be used, e.g. as an information tool for internal and/or external use (employees, customers, investors, etc.), and as a decision-making tool for human resource management (investments in human resources as well as personnel management in general).

In determining the relationship between HCA and the Assessment of Acquired Learning

The return on in investment in human capital become of more value Prior Learning Assessment (PLA) and the learning record, PLA offers to individuals reduced risk of investing in human capital. For firms, it makes HCA simpler and less expensive. For governments, there is the incentive of more efficient expenditure allocation during times of fiscal pressure. PLA "renders knowledge acquisition methods neutral," giving all forms of learning equal chances at being validated the OECD averred,

The PLA has the general impact of reducing the transaction costs both for individuals seeking to Invest in human capital or enter into a contract to rent their skills and for the firm's internal and external labor market decision making. Using PLA to reduce the cost and duration of incremental human capital investments relative to an individual's existing asset base is a contribution to efficient allocation of individual resources and investment incentive that reflects rates of return to recurrent education. the OECD asserts that to reap the benefits of PLA and human resources accounting practices, there should be means to strengthen market valuation of training and competences and developing a system for measuring competences designed to favour modular and continuing learning, and "reduce the lumpiness of investment imposed by the current certification system" thus the assertion is to reduce the overbearing on knowledge based training that emphasis certificate as the bedrock of competence and training more over for maximum gaining from human capital development firms must be encouraged to capitalize, collateralize and amortize knowledge; Work organization must also give clear title to well-defined competences through universal institutions for assessment and broadly recognized mechanisms for financial accounting; there should be transparency in labour contracting by revealing employee assets and employer benefits for maximum benefit firms must validate alternative learning acquisition. The work of Drucker and Reich (   ) on human capital accounting revealed that firms and governments are making choices and using resources to invest in the acquisition of human capital based on signals.

CEDEFOP Report (1998) have identified three ways of solving the policy problems relating to measurement of human capital training value in the organization this include the voluntary market-based method (the ISO standard method), i.e. develop a consistent framework which can be operational across sectors and countries and promote this through a rewarding and image campaign. There is also the voluntary rewarding method (the Investing in People method in the United Kingdom), i.e. develop a consistent framework supported by rewarding mechanisms once it is introduced and approved at enterprise level (enterprises pay for their training evaluation whether they meet the standard or not). Third is the compulsory method (the Green accounting method in Denmark), i.e. identify disclosure on human resources as a societal concern and prepare (inter-)national regulations

Human Capital and Performance

Recognition of human capital value can be of import in relation to the organization performance, human capital being a strong assets of the firm should necessarily be of value to the performance of the firm however, most time the attempt to establish a causal relationship between various human resource management (HRM) practices and organization performance have proved to be problematical. It may be intuitive to suggest that "good" HRM practice will improve organizational performance, but this has been difficult to prove conclusively, given the many confounding variables. It is even possible to suspect a reverse causation that the profitable firms can afford to treat their employees well.

Benefit of human capital accounting

It is worth noting that measurement of human capital is likely to provide useful information both to management and other stakeholders of the firm. several benefit could be adduced to accrue form the recognition of the value of human capital in the estimation of the firms assets, some of these includes Measurement of business performance, based on all the assets employed, rather than just those that can be measured readily in money terms; another is the allocation of personnel on the basis of most valuable to most critical tasks; there is also the comparison of the use of labour as against the use of other resources, such as machinery. Estimation of the human capital value would be of benefit in the consideration of the effectiveness of training and development expenditure and of business valuation for take-over and merger purposes it will also benefit the firm in the provision of a basis for more appropriate calculation of wages and salaries and in the setting of human resources policies.

Research problem

The basic problem of human capital valuation is cardinal to human capital management , today most firm do not want to invest in human capital development due to quick waste nature of human capital, also the basis of human capital management is the valuation process of human capital and how to account for the value in their financial report. However the there is no acceptable way of evaluating human capital for financial record purpose, it is a wasting assets of a long term nature and at the same time it asset nature can not be adequately quantified in their financial terms except treated as an expense the problem therefore with human capital value is that while it is variously regarded as assets but it is treated as expenses in their financial treatment.

Method of study

The study made use of descriptive method of data collection. The survey method using standard questionnaire to gather necessary data was used, the questionnaire was designed to gather relevant data relating to human capital accounting.

The judgmental sampling technique was adopted since the opinion of expert and professionals were needed and the fact that the total population of the study cannot be determined. Lagos state was selected for the purpose of the study; Ikeja, Ojo and Lagos Island local government were selected for the study. Seventy questionnaires were distributed in all, of which sixty was retrieved of which only fifty-six were usable. The chi-square, a non-parametric method of data analysis was adopted using a 5points likert-scale technique starting with strongly agreed to strongly disagreed with scale of 5,4,3,2,and 1 respectively.

Analyses and Interpretation of Study
Meaning Ranking

		Mean	**Standard deviation**
1	Var 004	2.6077	0.49281
2	Var 001	3.3929	0.49281
3	Var 006	3.3929	0.75593
4	Var 003	3.3929	0.40089
5	Var 002	3.1964	0.74881
6	Var 009	3.1964	0.74881
7	Var 005	3.000	0.000
8	Var008	3.000	0.63246
9	Var007	2.6071	0.49281

The table 1 above is the table that shows the mean ranking of the variables, the determined at 3.17 -_ 3.2. thus all variables with mean above and while all variables with mean less than 3.2 are classed as less important to the research at hand thus, var004, var001, varoo6, varo03, var002, and var009 are of very important value, these variable, very important value, these variable, var004 remain most valuable while var001 was next in ranking followed by record and var002 and var009 in representative order of value. The earn value able of all the variable is var007. The table also show the standard deviation of the variables, var003 has the highest standard deviation, it has neither a rate is var009 with S.D. of 0.748. it means respondent are more divergent in their view on the variable the least standard deviation is var005 with a standard deviation of 0.000, while 89 suggest that respondent are least divergent on their opinion on the variable.

Hypothesis Table

Variables	X^2	Significant level
Var001	2.521	
Var002	20.643	X
Var003	4.750	Xx
Var004	2.571	
Var006	2.571	
Var007	2.571	
Var008	18.893	X
Var009	4.750	Xx

Note: x (one asterisk) connote accept at 5%,   Xx (asterisk) connote accept at 10%
The variables tested were done at 5% and 10% significant level respectively. Var002 and var008 were accepted at significant level of 5% which is a strong acceptance of the variable these variables were the most valuable variable and other variables were tested at 95% confidence level. Var003 and var009 were all accept at 10% significant level that is at 90% confidence level. All other variables were rejected at both 5% and 10% significant level.

Summary and Conclusion

Summary

The study estimates the relative importance of human capital value in relation to the value of the firm. The following are the findings from the study

1. Human capital value should be estimated by productivity rather than certificate and training. Many emphases should be placed on human capital productivity within the firm.
2. The study discovered that human capital value should be best accounted using discounting future wages method of evaluation.
3. The study also revealed that both qualification and training should not be the bases of accounting for the value of human capital.
4. It was accepted that human capital should be classified as long term assets of the firm and their value should be capitalized rather than expense in the profit and loss account of the firm
5. The human capital value should be accounted for in the financial report of the firm as depreciable assets over the years rather than expense in the profit and loss account.

Conclusion

The study is an attempt to estimate the value of human capital and the treatment it should be accorded in the balance sheet and profit and loss account of the firm. This study concluded that human capital of the firm is the most value asset of the firm, it should not be therefore treated in value as expenses, rather as an asset, as asset of the firm it should be evaluated on the bases of discounted future wages method and should be capitalized in the balance sheet as depreciable asset of the firm, the value however should not be stated at replacement cost value. The value should also not be based on qualification and training but on productivity and value to the firm. This agreed with the principle of talent management of human capital (**Kehinde,** 2011). Conclusively human capital should be treated with value and esteem in the work of organization

Recommendation

1. Work organization should decide strategic method of evaluating human capital in their firm based on productivity and should be compensated rewarded as such.
2. Talent management should be given utmost value in the firm and human capital should be regarded as talent of the firm and should given topmost priority.
3. Organization should begin the capital of the firm to improve on the market value of the firm. Since organization leadership as a basic fundamental of the firm in the capital market.

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