



Human Resources Accounting Practices in Indian Banking : An Exploratory Study

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Abstract: Indian Banking is as old as any other banking system in the world and it is following various Human Resources Development (HRD) practices. The latest trend in HRD practices across the world is Human Resources Accounting (HRA) and today every organization is looking to understand their HR value in monetary terms as well. The banking industry which is service oriented and depends on mainly Human Resources (HR) is no exception to this trend, and must look into their HR valuations particularly due to changing economies and business models where mergers, acquisitions and takeovers have become the order of the day.

The present study focused on finding out and understanding the HRD practices of banking in India, with a special emphasis on HRA practices. Primary data were collected through interactions with various employees working in the HR departments of banks and secondary data were collected from various published documents, such as financial statements, journals, and other periodicals. The study's main findings were that: (1) Each bank has its own methodology in HRD practices for developing their HR; (2) No single bank is using HRA as a tool in the organization for HR valuations; (3) The majority of the officers is not aware of the availability of such a tool for HR development; and (4) No specific/separate data are captured by the banks for the purpose of HRA.

It was concluded that Indian banks need to focus on HRA practices for developing their HR in a systematic and organized way, to promote their HR as Intellectual Capital and to give it a prominent place in their financial reporting.

Keywords: HRD, HRA, Intellectual Capital, Banking

Introduction

The debate on the significance, validity and reliability of including human resource in the asset column of the balance sheet of a commercial organization is not new. While one school of thought argues for quantification of the HR as an asset, the other group dismisses the very thought of assessing the all-pervading intangible asset as it is beyond valuation and, in fact, invaluable. Nevertheless, attempts have been made by various researchers to quantify the HR by an array of permutations and combinations. Some have put forward certain calculations such as SPE (Sales Per Employee), RR (Recovery Rate), Utilization percentage, PpH (Profit Per Head) and CpP (Compensation Per Profit) while some others have advocated CIV (Calculated Intangible Value) method and MVA (Market Value added) approach equating HR with Intellectual Capital. But the predicament of the accountant still lingers, as there is no fool-proof formula to quantify the omnipresent human resource without which no organization can come into existence (Raju et al., 2004).

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Research Objectives

There were two research objectives that were addressed in this study:

1. To investigate different tools and techniques applied by selected Indian banks in identifying the Human Resources Value (HRV) in their organization; and
2. To examine the HRV reporting practices of selected banks in India

Rationale

Why HR Accounting?

The growing significance in most organizations of HRD is reflected in the "belief that the management of people is now a key element in the strategic planning of any organization" (Roslender & Dyson, 1992, p. 314) and the view that the aim of HRD is "to contribute to the value of the organization by optimizing the value of its human assets" (Flamholtz, 1999, p. 12). In the globalization of competition where competing through cost is not enough and so, for many organizations, future profitability lies in the skills and capabilities of employees, with the result that the development of people (resource-based strategies) becomes the new source of competitive advantage (Sloman, 1999). In the changing nature of management, managers are "increasingly becoming 'facilitators' of knowledge-intensive companies' most valuable assets: human and intellectual capital" (Flamholtz and Main, 1999: 19). A positive association has been established between high commitment management practices and the financial performance of organizations (Huselid, 1995; Wood, 1999). Sustainable growth comes through the organization's ability to develop what are its most valuable, rare and difficult to imitate resources (i.e., people) and to use these resources in what has become known as the 'value-based' theory of competitive advantage (Boudreau, 1990). The emerging evidence supports the view that managing human resources does lead to tangible returns, making the pressure to measure the accomplishments of the HR function even more intense (Pfeffer, 1997). This has led to viewing human beings as human resources, resource being defined as the available means to accomplish a goal. In the present age, such is the importance attached to human resource that it is considered to be the key asset of any company, the determinant factor of success in today's competitive arena. Despite this change, human resource has always been considered as a "soft" issue, an intangible whose impact could only be felt not seen as contrasted to other resources like capital, raw materials etc. whose contribution could be measured in tangible monetary terms. It was thus but natural that conventional methods of financial accounting neither formally did not record investment in employees, nor did they deal with issues relating to the measurement, valuation and accounting of human resource. Recently, there has been advancement in this area with many models being developed to carry out HRA (Flamholtz, Bullen, & Hua, 2002).

HRA seeks to measure the abilities of all employees in a company at all levels to produce value by way of that HRA is an upcoming practice across the world, which is more suitable for knowledge based and / or service oriented industries. The concept is much useful in Mergers and Acquisitions since valuation of assets is vital and human resource is no exception. Taking the measurement of and accounting for HR into 'something of a renaissance' (Roslender, 1997, p. 9), is the view that "organizations take seriously only what they can measure — and measure the things only they are serious about" (Johanson and Larsen 2000: 170). The challenge to be grasped is one of finding a way to value 'the intrinsic diversity in the worth of people' (Mayo, 2000:5). While 'putting people on the balance sheet' may be the dominant image of HR accounting for many (Flamholtz 1999:3) there is more to it than that.

Although HR accounting has been plagued by the difficulties of measurement, its aim is to accomplish two things:

- to provide a way of thinking about people as valuable organizational resources and
- to act as a decision-making tool providing the necessary information to effectively manage and develop such a valuable resource (Flamholtz, 1999; Johanson and Larsen, 2000; Roslender & Dyson, 1992; Scarpello & Theeke, 1989).



In this respect HR accounting is 'clearly of much greater importance than simply finding a means of putting people on the balance sheet' (Roslender & Dyson, 1992: 319)

Present Reference

It is a fact that due to implementation of Financial Sector Reforms in India, the Indian banking industry is currently undergoing a sea change. Since the sector is also opening up for Foreign Direct Investment (FDI), it is more prone for takeovers and mergers. Hence there is every need for the Indian banking industry to look into the valuations, especially HR valuations, since HR valuations play a major role at the time of mergers and/or acquisitions.

Hypothesis

Ho: In the Indian banking industry, HRA is practiced and reported in the banks' financial statements.

Research Methods

Data Collection

1. Primary data were collected from the HR Departments of selected Indian banks by using a questionnaire; and
2. Secondary data were collected from published documents, such as annual reports, periodicals, magazines and Reserve Bank of India reports

Procedure

1. Qualitative and quantitative analysis was conducted of the primary as well as the secondary data collected from various sources; and
2. Evaluation of the various HRA tools and techniques applied by the banking sector was carried out and compared with the standard models to understand the superiority of the banking models over standard models

Source of Data

The sample was drawn from 19 (all) nationalized banks' HR departments, since these banks are subject to more regulations and disclosures and control nearly 80% of the country's banking business. The banks are identified through random sampling. (Annexure – 1)

The questionnaire was sent to the Heads of Human Resources / Personnel Department of each bank for responding and the response is 100%. The questionnaire was developed exclusively for this study and was validated by the expert opinion

Present Banking scenario ³

Strengths	Weakness
<ul style="list-style-type: none">• High skilled personnel in middle and low levels in the banks.• Aggression towards the development of the existing standards• Strong regulatory impact by central bank to all banks for implementation• Presence of intellectual capital to face the change in implementation with good quality	<ul style="list-style-type: none">• Poor technology infrastructure• Presence of more number of smaller banks that would likely to be impacted adversely.• Poor compensation system• Poor talent management

³ Source: Jagannath Mishra & Pankaj Kumar Kalawatia: Basel II: Challenges Ahead of the Indian Banking Industry 2008



Opportunities	Threats
<ul style="list-style-type: none">• Availability of fresh talent to strengthen the bank operations.• Increasing risk manage expertise• Need significant connection among business, credit & risk management and information technology	<ul style="list-style-type: none">• Inability to meet additional capital• Requirements• Huge investment in technologies• Entrance of foreign banks to capture talent HR• Increasing the cost of human capital.

In the present context, it can be observed that the Indian banking industry's success is depending more on the success of its HRD policies and practices.

Contemporary Context

HRA is gaining momentum in the new generation accounting practices. This concept can be applied in services and knowledge based industry like banking and software industries in valuation of assets as the total performance of these industries is HR-based. The objective of HRA is not just the recognition of the value of all resources used by the organization, but it also includes the management of HR so that the quantity and quality of goods and services are enhanced. The basic objective behind HRA is to facilitate the effectiveness and efficiency of HR. That is where it gets associated with Human Resource Development. Without systematic HR data as part of the management information system, it is not possible to draw out meaningful HRD programmes. HRA also helps in decision making in the following areas.

1. Direct Recruitment vs Promotion
2. Transfer vs Retention
3. Retrenchment vs Retention
4. Impact of budgetary controls on Human Relations and Organizational Behavior.

For any meaningful HRD policy, it is very important to have systematic HRA procedures in the organizations. (Verma,2006). Banking is no exception for HRM and HRD practices. Since banking is service oriented and its assets are managed by the most important asset, *i.e.* Human Resources, there is every need to account it. It is very important and apt time for the Indian banking industry to adapt HRA practices and implement.

Since banking is opening for FDI the industry is prone to mergers and takeovers, therefore valuation of assets including Human Resources is an urgent need. Hence the study of HR accounting practices in Indian banking.

Benefits of HR Accounting

The benefits of HR Accounting are listed below:

1. The HR accounting system helps to calculate and disclose the value of human resources. This helps in proper interpretation of Return on Capital Employed, especially on Human Resources. Such information would give a long term perspective of the business performance which would be more reliable than the Return on Capital Employed under the conventional system of accounting.
2. This accounting practice also helps in proper managerial decision making like "direct recruitment versus promotions; transfer versus retention retrenchment or relieving versus retention; utility of cost reduction programs in view of its possible impact on human relations and impact of budgetary control on human relations and organizational behavior. Thus, the use of HRA will definitely improve the quality of HRD and, thereby, improvement in the performance of the organization.
3. The HRA also serves social purposes by identifying human resources as a valuable asset which will help prevention of misuse and under use due to thoughtless or rather reckless transfers, demotions, layoffs and day-to-day maltreatment by supervisors and other superiors in the administrative hierarchy; efficient allocation of resources in the economy ; efficiency in the use of



human resources; and proper understanding of the evil effects of avoidable labor unrest / disputes on the quality of internal human resources.

4. The system of HRA would, no doubt, pave the way for increasingly productivity of human resources, because the fact that a monetary value is attached to human resources and that human talents devotion and skill considered as valuable assets and allotted a place in the financial statements of the organization, would boost the morale, loyalty and initiative of the employees, creating in their mind a sense of belonging towards the organization and would act as a great incentive, giving rise to increased productivity.

HRD Practices of Indian Banking.

To understand the HRD practices of Indian banks, the data were collected through primary as well as secondary sources. The primary data were collected through interactions with various HR employees working in banks and the secondary data were collected from published documents, such as annual reports, journals and magazines. As suggested by the RBI, banks follow various reporting practices and a few of them are furnished below.

In the recent past, a number of developments have taken place in the banking industry to improve the transparency in the banking sector. Recognizing considerable divergence amongst the financial institutions in the nature and manner of disclosures made by them in their published annual reports, the disclosure norms were introduced by Reserve Bank of India for the banks with a view to bringing about uniformity in the disclosure practices adopted by them and improving the degree of transparency in their affairs. The Institute of Chartered Accountants of India (ICAI) has issued a series of Accounting Standards in the recent past to improve the accounting and disclosures made by the enterprises. These standards are applicable to all the banks.

There are about 36 different items on which the banks have to disclose the information in their financial statements and the details are as follows:

1. Capital
2. Repo Transactions
3. Non-SLR Investment Portfolio
4. Derivatives
5. Forward Rate Agreement/ Interest Rate Swap
6. Exchange Traded Interest Rate Derivatives
7. Disclosures on risk exposure in derivatives
8. Non-Performing Assets
9. Particulars of Accounts Restructured
10. Details of financial assets sold to Securitisation/ Reconstruction Company for Asset Reconstruction
11. Details of non performing asset purchased/sold
12. Provisions on Standard Asset
13. Asset Liability Management - Maturity pattern of certain items of assets and liabilities
14. Exposure to Real Estate Sector
15. Exposure to Capital Market
16. Risk Category wise Country Exposure
- 17 Details of Single Borrower Limit (SGL), Group Borrower Limit (GBL) exceeded by the bank
18. Unsecured advances
19. Amount of Provisions made for Income-tax during the year
20. Disclosure of Penalties imposed by RBI
21. Accounting Standard 5 – Net Profit or Loss for the period, prior period items and changes in accounting policies



22. Accounting Standard 9 – Revenue Recognition
23. Accounting Standard 15 – Employee Benefits
24. Accounting Standard 17 – Segment Reporting
25. Accounting Standard 18 – Related Party Disclosures
26. Accounting Standard 21- Consolidated Financial Statements
27. Accounting Standard 22 – Accounting for Taxes on Income
28. Accounting Standard 23 – Accounting for Investments in Associates in Consolidated Financial Statements
29. Accounting Standard 24 – Discontinuing Operations
30. Accounting Standard 25 – Interim Financial Reporting
31. Other Accounting Standards
32. Provisions and contingencies
33. Floating Provisions
34. Draw Down from Reserves:
35. Disclosure of Complaints
36. Disclosure of Letters of Comfort (LoCs) issued by banks

The RBI also categorically stated in the guidelines of July 1, 2009 that the disclosures explained in their guidelines are only minimum requirements and the banks on their own initiative are encouraged to make more comprehensive disclosures than the minimum required under the circular if they become significant and aid in the understanding of the financial position and performance of the bank

We examined the latest (FY2009-10) financial statements of the selected public sector and also private sector Indian Banks, with specific reference to the disclosure practices of banks and follow up of RBI and ICAI guidelines. It was found that no bank is disclosing any information related to HR Valuations.

Results, Recommendations and Conclusion

Results of the Study

From the current study it has been understood in India no bank is practicing and reporting HR accounting in their financial statements and hence the hypothesis is rejected

Recommendations and Conclusion

HRA is a recent concept particularly for Indian corporations and has achieved very high importance in the globalized environment, especially when mergers and acquisitions are on cards. Every public sector organization must focus in this area of financial reporting. The following suggestions are made for implementing HRA in the respective organizations:

1. Though RBI has made 36 different items as mandatory for all banks to disclose, they are only keeping in view of the interest of the depositors and / or investors. But no disclosure is considering employee valuation. RBI should include HRA also as a disclosure item;
2. Corporate trainings should be conducted to create awareness among all the employees and more particularly to the top management;
3. The accounting practices shall be suitably modified to collect relevant data for valuing Human Resources and included in all financial reports; and
4. A suitable model should be adopted to value the HR of Indian banks.

Limitations

The Indian banking sector employs different structures, such as cooperative banks, rural banks, private sector banks, public sector banks and foreign banks. Therefore bringing uniformity in the data collected from different organizations is a limitation in such a diverse system.



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