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AN ANALYSIS OF THE CONTRIBUTION OF HUMAN RESOURCE ACCOUNTING DISCLOSURE TO THE QUALITATIVE CHARACTERISTICS OF FINANCIAL REPORTING

by

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Abstract

Recent economic development has brought out the importance of human resources as a value creator, necessary for economic and organizational growth. Economic development requires improvements in human resource accounting (HRA) practice and research to ensure that financial reports succinctly provide stakeholders with the necessary information about human resources to help improve decision-making. Despite the abundance of empirical evidence supporting the influence of HRA information on investment and other decisions, HRA is yet to be incorporated into conventional accounting. Reporting entities provide HRA information voluntarily because the current accounting standards and regulations do not mandate reporting entities to adopt HRA. Although HRA and research have drawn the attention of researchers and practitioners, researchers have not paid much attention to the contribution of HRA disclosure to improvement in financial reporting quality (FRQ). This paper argues that there is a need for empirical studies on the contribution of HRA disclosure to FRQ. This paper also argues that one of the ideal ways to investigate the contribution of HRA to FRQ is to measure FRQ using qualitative characteristics. Qualitative characteristics are a more appropriate measure of FRQ because they can take care of the financial and non-financial information in a financial report. Because HRA disclosure includes both financial and non-financial information, measuring FRQ using qualitative characteristics is more appropriate. Additionally, qualitative characteristics are the direct measure of FRQ.

Keywords: Human resource accounting, Financial reporting quality, Voluntary disclosure, Qualitative characteristics of financial reporting

INTRODUCTION

The recent transformation in the world economy has brought out the importance of human resources as a factor in the determination of corporate success. From the industrial revolution era to today's knowledge economy, human resources have continued to attract growing attention from both researchers and practitioners (Arkan, 2016; Ibukun-falayi & Falayi, 2014; Sharma & Shukla, 2010). Firms strive to attract, employ, and retain the best employees to help them achieve their organisational goals (Ibukun-falayi&Falayi, 2014). Furthermore, firms all over the world invest significant organisational resources in training and development of their employees (Abdi et al., 2020).

In trying to remain in tune with the changes in the global economy, some authors advocated for the introduction HRA (Kaur et al., 2014; Sharma & Shukla, 2010). The target of HRA is to ensure adequate and proper accounting of human resources from the accountants' point of view and the integration of HRA information into the financial reports (Ijeoma, 2015).

HRA is bedevilled with numerous problems, ranging from conflicting conceptualisations to a lack of an acceptable valuation model and an absence of accounting standards (Bonsu et al., 2019; Arkan, 2016). In many countries, the reporting of HRA in the financial statements is voluntary (Verma & Kirti, 2019; Hay et al., 2018; Petera & Wagner, 2017). Each reporting entity decides what information to provide and how to provide it, resulting in a diverse means of reporting HRA information. As of today, HRA is yet to be integrated fully into the framework of financial reporting (Akintoye et al., 2018).

There are many studies on HRA. These studies mainly concentrated on the development of the concept and finding solutions to some of its problems (Bonsu et al., 2019; Arkan, 2016; Sharma & Lama, 2014; Kashive, 2013). Other studies investigated the relationship between HRA and some aspects of financial reporting, like organisational performance (Asika et al., 2017; Jesuwunmi et al., 2017; Cherian & Farouq, 2013). Few studies have looked into the role of HRA in financial reporting quality (Odunayo & Festus, 2020; Abubakar, 2011).

This paper observes that the lack of literature on the relationship between HRA and FRQ calls for an investigation. The paper particularly emphasises the need to investigate the contribution of HRA to FRQ using the qualitative characteristics of financial reporting as the primary measure of FRQ. The paper observed that few studies among the few prior studies on the relationship between HRA and FRQ measured FRQ using the qualitative characteristics of financial information. The paper argues that the qualitative characteristics are a better measure of FRQ to be used in determining the contribution of HRA to FRQ. The paper argues that since HRA disclosure comprises both financial and non-financial information, measures of FRQ are dependent upon the financial information presented in the financial reports, which may be inadequate for assessing the contribution of HRA to FRQ.

Human Resource Accounting

Organisations invest a significant amount of money in hiring, training, and developing the capacity of their human resources (Janshanlo et al., 2019; Kanade & Harwani, 2018; Wyatt & Frick, 2010). Investments in human resources aim to help organisations achieve their organisational goals and gain a competitive advantage over their competitors (Kanade & Harwani, 2018; Justus & Christopher, 2016; Chaudhry & Roomi, 2010). The introduction of HRA is to take care of the peculiarities of human resources for accounting and financial reporting purposes.

According to Sharma and Shukla (2010), HRA "is a process of identifying and measuring data about human resources. It means accounting for people as an organizational resource" (p. 131). Bansal et al. (2019) describe HRA as "the process of identifying, measuring data about human resources and communicating this information to interested parties" (p. 1). Sharma and Shukla (2010) posit that the concept of HRA holds that employees are valuable resources of an organisation and that information about these resources is useful for making sound and effective organisational decisions. Arkan (2016) maintains that HRA "helps management frame policies for human resources especially where it is necessary to identify, measure and disclose data about the people within an organisation, where they are recognised as an accounting resource" (p. 174). As a result, HRA is an important tool for gathering relevant information about human resources and decision-making.

The importance of HRA as a tool for generating information is not limited to management information alone. For instance, HRA information plays an important role in investment decisions and has a significant effect on share prices (Hendricks, 2014; Abdullahi et al., 2012; Okpala & Chidi, 2010). The impact of HRA information on many factors implies that HRA information is useful to diverse stakeholders of reporting entities.

Financial Reporting Framework and Human Resource Accounting

Although there are arguments against regulation (Bushman & Landsman, 2010), present-day financial reporting is regulated (Scott, 2015; Atrill & McLaney, 2011; Bushman & Landsman, 2010). Reporting entities comply with rules, regulations, and principles in preparing and presenting their financial reports. Regulators of financial reporting use two mechanisms to achieve a controlled reporting environment. These mechanisms are accounting rules (standardisation, principles, and conventions) and legislation (Scott, 2015).

One of the mechanisms for regulating financial reporting is the use of accounting standards as a part of the accounting rules (Elliott & Elliott, 2017; Scott, 2015). Before the adoption of the International Financial Reporting Standards (IFRS), many countries used to have distinct accounting standards. Reporting entities must comply with these national standards in the preparation of their financial statements (Elliott & Elliott, 2017; Scott, 2015). These country-specific standards ensured the standardisation of financial reports within a country. For example, in Nigeria, before the adoption of IFRS, the Nigerian Accounting Standard Board (NASB) was the body saddled with the responsibility of issuing accounting standards known as Statement of Accounting Standards (SAS) (Aliu, 2019; Micah et al., 2012) while, at the international level, the International Accounting Standards Committee (IASC) issued the International Accounting Standards (IAS) (Ballas et al., 2019; Kashive, 2013). The two sets of accounting standards shape the financial reporting of organisations.

The establishment of the International Accounting Standards Board (IASB) in 2011 paved the way for the issuance of International Financial Reporting Standards (IFRS) (Scott, 2015). The target of IFRS is not just to achieve regulation in financial reporting but also to ensure harmonisation and convergence of standards and practices (Elliott & Elliott, 2009; Scott, 2015; Godfrey et al., 2010). Elliott and Elliott (2009) summarise the major philosophies behind the setting up of international standards thus: "The main reasons for the development of international standards is that it makes it easier to raise cross-border finance and to compare performance" (p. 154). The adoption of the IFRS has resulted in a significant level of financial reporting harmonisation and improvement in FRQ (Shuraki et al., 2021; Prihatni et al., 2016).

Apart from the use of accounting rules, many countries use legislation to regulate financial reporting. Examples of such legislation are the Sarbanes–Oxley Act in the United States (Krishnan et al., 2020; Rubin & Segal, 2011) and the Companies and Allied Matters Act in Nigeria (Okpala & Chidi, 2010). Most of these laws are meant to ensure transparency and accountability in financial reporting (Ballas et al., 2019; Rubin & Segal, 2019).

Disclosure in Financial Reports

Reporting entities transmit financial information to users of accounting information through presentation and disclosure in financial statements (Koppeschaar et al., 2019). As a result, disclosure has become an additional means of presenting accounting information in financial reports (Elliott & Elliott, 2017). The inclusion of some additional information not reported in the main statements of a financial report is referred to as disclosure (Elliott & Elliott, 2017). Dyana and Kesavan (2015) describe disclosure as "the process of providing information about items in the financial statements…" (p. 1). A variety of disclosures are expected to be included in financial reports. These disclosures are often in the form of notes that give further explanations of the material in the main statements (Elliott & Elliott, 2017). Dyana and Kesavan (2015) explain that reporting entities provide disclosure "via footnotes, supplementary schedules, or other means" (p. 1).

According to Bragg (2018), the concept of full disclosure, which mandates organisations to include additional information in their financial reports, has received much attention in accounting standards. To comply with full disclosure requirements, a reporting entity must include additional information in or alongside its financial reports. These extra details should be those that may affect the users' interpretation of the financial reports (Atrill & McLaney, 2011). In general, accounting standards have expanded the concept of full disclosure requirements significantly (Bragg, 2018). Notes to the accounts give extra information to make the financial reports more complete. Furthermore, the notes include other information that cannot be presented in either the income statement or the statement of financial position based on conventional accounting rules (Bragg, 2018).

An analysis of the disclosure practices of reporting entities would suggest that the disclosure can either be mandatory or non-mandatory (Elliott & Elliott, 2017; Dyana & Kesavan, 2015). Further analysis of the disclosure practices of reporting entities would reveal two types of disclosures: financial and non-financial (Elliott & Elliott, 2017; Dyana & Kesavan, 2015; Kashive, 2013).

Mandatory disclosure is a type of disclosure that accounting standards and legislation require reporting entities to make (Bragg, 2018; Koppeschaar et al., 2019; Elliott & Elliott, 2017). Reporting entities comply with the provisions of accounting standards and relevant legislation. Some reporting entities make disclosures beyond what they are mandated to disclose (Kashive, 2013). Disclosure over and above the mandatory disclosure requirements is non-mandatory and is called "voluntary disclosure" or "discretionary disclosure" (Fakoya & Lawal, 2020). Asserting the need for voluntary disclosure, Atrill and McLaney (2011) explain that reporting entities "(... produce a considerable amount of accounting information for managers, which is not required by any regulations.) Presumably, the cost of producing this additional accounting information is justified on the grounds that users find it useful" (p. 5).

Mandatory and voluntary disclosures can either be financial disclosures or non-financial disclosures (Elliott & Elliott, 2017; Dyana & Kesavan, 2015; Kashive, 2013). In financial reporting, financial disclosure refers to the provision of additional financial information in financial reports using money measurement (Emmanuel et al., 2019; Naghshbandi et al., 2016). On the other hand, non-financial disclosure refers to the disclosure of additional information in financial reports by using non-financial indicators (Branco et al., 2010; Emmanuel et al., 2019). Non-financial metrics include "indices, scores, ratios, counts and all other information that is not accounted for in primary financial statements" (Kashive, 2013, p. 115).

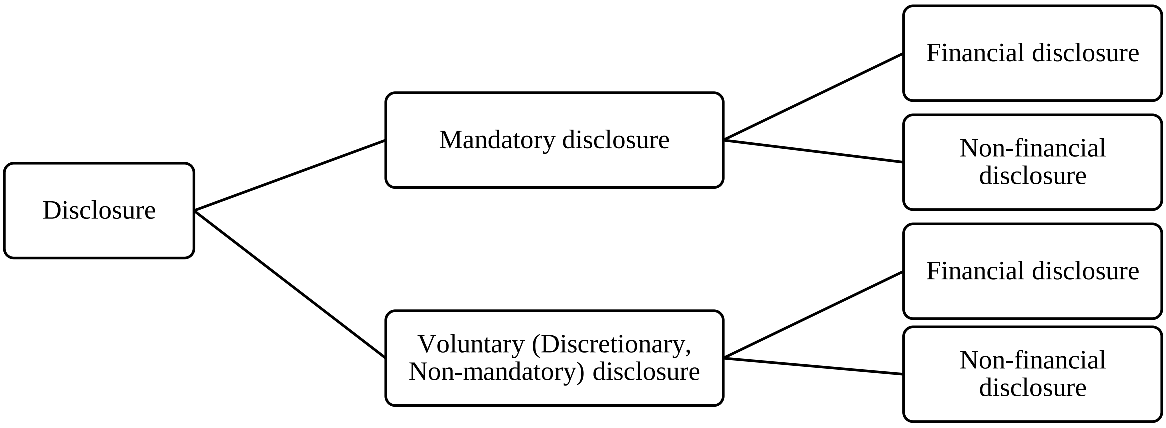

Figure 1: Types of disclosures in financial reports

Figure 1 shows the typical classification of accounting disclosures in financial reports. Apart from disclosing information to fulfil the requirements of a standard or legislation (mandatory disclosure), a reporting entity can make additional disclosures as part of its voluntary disclosure. Each of the two types of disclosures can either be of financial or non-financial information.

Nature of Human Resource Accounting Disclosure

There are no accounting standards for HRA (Chatterjee & Chatterjee, 2018; Ibukun-falayi & Falayi, 2014; Jesuwunmi et al., 2017; Kashive, 2013). Therefore, reporting entities provide HRA information as part of their voluntary disclosure in the financial reports (Kaur et al., 2016; Micah et al., 2012). Hence, under conventional accounting practice, HRA information is mostly disclosed. Except for the cost of recruitment, training, and salaries, which are expensed through the income statement, most of the information relating to HRA are not reported in the main statements of financial reports (Bello & Micah, 2021; Sarkar et al., 2016). Hence, most of the HRA information are reported in the note to the accounts or supplementary statements in the form of disclosure (Bello & Micah, 2021; Dey& Sarkar, 2015; Petkov, 2010; Sarkar et al., 2016).

Reporting entities provide different items of disclosure as part of their voluntary HRA disclosure (Akintoye et al., 2016; Syed, 2009). The variation in HRA practices and HRA disclosure may not be unconnected to the fact that HRA has not been standardised yet (Jesuwunmi et al., 2017; Ibukun-falayi & Falayi, 2014; Rahaman et al., 2013). A review of the items reporting entities report as part of HRA disclosure as reported in prior studies show that the disclosure items are both financial and non-financial HRA information. Table 1 contains a summary of the items used in some studies as HRA disclosure information in the financial reports.

Table 1: HRA disclosure items

S/N	Disclosure Items
1	Employment report
2	Separate HRA statement
3	Employees' value addition
4	Total Value of Human resource
5	Value of HR per Employee
6	Valuation Model Used
7	Value Added per Employee
8	Human resource policy
9	Training and development
10	Management succession plan
11	Human resource development fund
12	Employees/workers fund
13	Employee categories
14	Age Wise Distribution
15	Group Wise Distribution
16	Gender Wise Distribution
17	Education Index
18	Employee Cost
19	Managerial remuneration
20	Retirement benefits
21	Performance Recognition
22	Superannuation fund
23	Other employees benefits

Sources: Akintoye et al. (2016), Micah et al. (2012) and Syed (2009)

A careful observation of the list of HRA disclosure items in Table 1 above indicates that the items contain both financial and non-financial HRA information. Therefore, HRA disclosure items comprise both financial and non-financial disclosure.

Financial Reporting Quality

The concept of FRQ is important in financial reporting. High-quality financial reports boost investors' confidence and the confidence of other decision-makers. FRQ leads to sound judgement regarding a company. According to Mahmoud (2017), FRQ improves transparency and enables more extensive disclosure in financial reporting.

The goal of FRQ is to guarantee that a firm's financial status and performance are accurately presented for investors and other stakeholders to make reliable and informed decisions (Herath & Albarqi, 2017). All things being equal, it might be claimed that high-quality financial reports give credible information and that decisions based on the reports are effective. Some authors have recommended improvements in FRQ. For instance, in a study involving listed oil businesses in Nigeria, Mahmoud (2017) advocates for improved FRQ, citing the fact that the accounting information supplied by reporting entities is valuable to investors. The study suggests that enhancing a company's FRQ will positively influence the market price of its shares on the stock exchange. As Herath and Albarqi, (2017) point out, the value-relevance of accounting information is determined by the quality of financial reporting.

Measuring Financial Reporting Quality

FRQ can be measured in a variety of ways (Martnez-Ferrero, 2014). Various FRQ metrics have been used in previous research. Except for the qualitative qualities of the FRQ, the majority of the other approaches rely solely on secondary data. Earning quality, accrual quality, accounting conservatism, value relevance model, specific elements in the financial report, and qualitative characteristics are some of the measures of FRQ used in prior studies (Beest et al., 2009; Alexios Kythreotis, 2014; Martnez-Ferrero, 2014; Tasios & Bekiaris, 2012).

A higher-quality financial report faithfully represents information that is relevant, reliable, comparable, understandable, and timely (IASB, 2018; Herath & Albarqi, 2017). Mahboub (2017) and Beest et al. (2009) observe that, except for the qualitative characteristics of the financial report as a measure of FRQ, the other measures have apparent deficiencies. Most of the other methods measure FRQ using financial information from balance sheets and income statements. The other methods do not take into account non-financial information in measuring FRQ (Mahboub, 2017; Beest et al., 2009). Akeju and Babatunde (2017) argue that "financial reporting quality does not only refer to financial information but also disclosures and non-financial information useful for decision-making included in the financial statement" (p. 3749).

Several prior studies adopted qualitative characteristics to measure FRQ. Omoro (2019) observes that "the qualitative characteristics have been used in many studies to proxy FRQ" (p. 875). Some of the studies that used qualitative characteristics to measure FRQ include Albawwat et al. (2021), Omoro (2019), Mahboub (2017), Mbobo and Ekpo (2016), and Beest et al. (2009). Some authors believe that the qualitative characteristics are a better indicator of FRQ since they take into account both financial and non-financial information in a financial report. Qualitative characteristics take into consideration all the aspects of decision usefulness identified in the IASB (2018) conceptual framework for financial reporting.

The IASB (2018) and Beest et al. (2009) identify six qualitative financial reporting characteristics. The qualitative characteristics are relevance, faithful representation, understandability, comparability, verifiability, and timeliness. The six characteristics are the accepted elements of FRQ (IASB, 2018). The six characteristics are further classified into fundamental and enhancing (Omoro, 2019; IASB, 2018; Beest et al., 2009). Fundamental characteristics are relevance and faithful representation. Comparability, verifiability, timeliness, and understandability are all enhancing characteristics (IASB, 2018). The enhancing characteristics improve the usefulness of information, but they do not transform non-useful information into useful information (IASB, 2018; Herath & Albarqi, 2017).

According to Herath and Albarqi (2017), relevance is concerned with the materiality and use of the information. Relevance is what makes knowledge useful. When information is relevant, it can affect the decisions of information users. Decisions are influenced by the predictive and confirmatory qualities of financial information (IASB, 2018; Herath & Albarqi, 2017). The relevance of financial information is heavily reliant on its capacity to give forward-looking, non-financial information. Such information should offer both fair value and feedback to users of the information on how key events influence the organisation (Mbobo & Ekpo, 2016).

The faithful representation of information is the second fundamental characteristic of financial reporting (IASB, 2018; Herath & Albarqi, 2017; Mbobo & Ekpo, 2016). Faithful representation means that an item properly reflects the substance it claims to represent. For information to be considered faithfully represented, the information should be thorough, impartial, and devoid of major misstatements and inaccuracies. However, measurement errors might have an impact on faithful representation (IASB, 2018).

One of the enhancing qualitative qualities of financial reporting is understandability (IASB, 2018). Understandability is attained via effective communication. The user of information judges whether a piece of information is understandable or not. As a result, the higher the degree of understandability, the better the user understands the content of a financial report (Herath&Albarqi, 2017). Understandability may be improved by carefully presenting and categorising information in the financial report. The use of graphs, charts, tables, and straightforward presentations helps in comprehending technical terms and jargon.

Comparability is also an enhancing qualitative feature of useful financial information. Comparability allows information users to compare and contrast financial and economic information in a financial report (Mbobo & Ekpo, 2016). Comparability provides users of the information with the opportunity to compare financial reports, cash flows, performances, and financial positions of different organisations. Information users can compare the information from a reporting entity's reports or reports with other firms' reports over time or with reports from other firms (Herath & Albarqi, 2017). To improve the comparability of information in the financial report, a reporting entity should be consistent in applying accounting policies and disclosing changes in the policies as well as identifying the consequences of the changes. Furthermore, the use of financial ratios can improve comparability (Herath & Albarqi, 2017; Beest et al., 2009).

Another enhancing qualitative feature of financial information is timeliness (Mbobo & Ekpo, 2016; Beest et al., 2009). Timeliness is about presenting information to decision-makers in a timely manner before the information loses its ability to affect their decisions (Mbobo & Ekpo, 2016).

Contribution of Human Resource Accounting Disclosure to Financial Reporting Quality
Many studies have reported significant improvements in FRQ as a result of IFRS adoption. For instance, Agyei-Mensah (2013) found significant improvement in the FRQ of listed companies in Ghana after the adoption of IFRS. For example, Kythreotis and Constantinou (2020), Habib et al. (2019), Osasere and Ilaboya (2018), and Aderin and Otakefe (2015) are among the studies that found an improvement in FRQ due to IFRS adoption.

Akintoye et al. (2016) are among the studies on the impact of IFRS adoption on HRA. Akintoye et al. (2016) found that IFRS adoption has no significant impact on HRA and HRA adoption. According to some studies, there is no specific IFRS on HRA. As such, authors like Akintoye et al. (2018), Asika et al. (2017), Omole et al. (2017) and Okoye et al. (2017) all called for the issuance of a specific accounting standard on HRA.

Although there are no specific IFRS provisions on HRA, reporting entities continue to make voluntary HRA disclosure. A question that comes to mind is: why do reporting entities continue to make voluntary HRA disclosures if IFRS and other financial regulations do not ask for it? Another question to ask is why did the IASB fail to issue a specific accounting standard on HRA? Given that IFRS adoption leads to improved FRQ (Habib et al., 2019; Osasere & Ilaboya, 2018), and IFRS adoption does not improve HRA (Akintoye et al., 2016), the answer to these questions will be critical in understanding the basis of the arguments of the HRA advocates who insist that there is a need to have a specific accounting standard on HRA. Therefore, one of the means of finding answers to these questions is to investigate the contributions of HRA to FRQ.

There are many empirical studies on HRA. Many of these prior studies concentrated on the different aspects of HRA. For example, some of the studies looked at how to develop valuation models and an accounting framework for HRA. Some studies in this category include Asein et al. (2019), Arkan (2016), Akintoye et al. (2018), Al Hanini (2018), and Moghadam et al. (2017). Other prior studies on HRA tried to identify and find solutions to the problems and challenges of the concept. Bonsu et al. (2019) and Naghshbandi et al. (2016) are in this category. There are also studies on the effects of HRA on profitability. Examples include Ofurum and Adeola (2018), Oko (2018), Amahalu et al. (2017), and Asika et al. (2017). Khan (2021), Inua, and Oziegbe (2018) investigated the impact of HRA on firm performance. There are many studies on various firm characteristics, including capital structure (Aggarwal, 2021), firm structure (Bello &Egbe, 2021) and firm characteristics (Kaur et al., 2016; Kusumastuti, 2021; Ojokuku & Oladejo, 2017). Olayiwola (2016) investigated the relationship between human capital costs and stock prices. Akintoye et al. (2016) examined the impact of adopting IFRS on HRA disclosure.

However, scrutiny of existing literature shows that there is a dearth of literature on the contribution of HRA to FRQ. Currently, there are very few empirical studies on the relationship between HRA and FRQ. Additionally, many of the few empirical studies on HRA and FRQ used indirect measures of FRQ. These few empirical studies did not measure FRQ using the direct measure of FRQ (qualitative characteristics). One of the few investigations into the relationship between HRA and FRQ is Odunayo and Festus (2020), who investigated the relationship between HRA and FRQ using ex-post facto research. Odunayo and Festus (2020) measured FRQ using accounting conservatism, earning quality, and earning smoothness. Another study on the relationship between HRA and FRQ is by Abubakar (2011). Like Odunayo and Festus (2020), Abubakar (2011) did not measure FRQ using the qualitative features of financial reporting.

CONCLUSION AND RECOMMENDATIONS

Accounting as a dynamic field (Ijeoma, 2015) cannot ignore the position and roles of human resources, which the dynamism of world economy have made manifest. As a value creator and a major determiner of the success of firms, human resources deserve special attention in accounting and financial reporting (Bello & Micah, 2021; Abdullahi et al., 2012). This is because information about human resources has been linked to investment and other critical decisions (Hendricks, 2014; Abdullahi et al., 2012). Current accounting practices allow reporting entities to report most of the information relating to human resources by way of disclosure only. Many reporting entities now take advantage of voluntary disclosure to report more human resources information. The voluntary HRA disclosure by reporting entities is an indication that the information is useful to their stakeholders. Despite this development (voluntary HRA disclosure), there are no accounting standards or regulations on HRA. Therefore, there is a need for empirical investigation into the contribution of voluntary HRA disclosure to the quality of financial reporting.

Although there are numerous studies on various aspects of HRA, there is a lack of studies on the contribution of this voluntary HRA disclosure of reporting entities to FRQ. This paper argues that empirical evidence would be valuable in determining whether the voluntary HRA disclosure practice of reporting entities adds to the quality of financial reporting or not. This paper argues that one of the most appropriate ways to measure FRQ in a study on the impact of HRA disclosure is the use of qualitative characteristics released by IASB (2018).

Researchers should look into the possibility of studying the relationship between HRA disclosure and FRQ using qualitative characteristics. This will help in ascertaining the contribution of HRA to FRQ. Furthermore, the results from such investigations will help shape HRA practice in the future.

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