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TOWARDS A MORE MEANINGFUL FINANCIAL STATEMENT

by
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Private enterprise companies have social and environmental responsibilities to employees, customers and the community. A measurement such as earnings per share is much too narrow and restricted to the proprietorial interests only. Very often, profitability, which seems to dominate the business world, is emphasised so much that it overshadows the social responsibility of corporate organisations.

Every company is required to prepare annual financial statements. Section 169 of the Malaysia Companies Act provides that the directors of every company must, in respect of each accounting period of the company, prepare a profit and loss account and a balance sheet as at the date at which any profit and loss statement is made up. Reports of the directors and auditors should be attached to the two financial statements. The financial statements are quantified statements attempting to convey to the users as to what was happening in the financial accounting year. At present, the usefulness of financial statements in fulfilling the users' needs is restricted because of the defects of measurement used. In times of escalating inflation, historical cost accounting fails to depict a true picture to the users. When reported figures are not related to current values, there may be over or understatement of performance as measured by profits and returns on assets.

The accounting problem, however, is not only confined to the problem of measurement. The technological revolution which has accelerated since the Second World War has altered the nature of accounting problems as well. The accounting problem is no longer limited to providing financial information about the activities of business organisations; the accounting problem in a technological society is the provision of information covering all aspects of human activity within the business organisation. Any firm has a relationship with its environment, securing its input from the environment and releasing its output to the environment. It is no longer only responsible to shareholders, but it has an environmental responsibility to employees, customers and the community as well.

In a complex business world, it is impossible to condense the entire annual economic activities (what more to say of its social and environmental activities) down to the few pages which make up the financial statements. Consequently, no set of financial statements will suffice to disclose every single important event that has happened during the accounting year. In many cases, events which may not have an immediate and apparent impact are simply ignored for accounting purposes. Why? The requirement of the concept of objectivity forbids it! Fortunately, realization has dawned upon some concerned accountants that companies have much more of a responsibility than just putting figures down in a financial statement. Non-quantifiable events, such as pollution to the environment, should not and cannot be shoved aside. More and more organisations are becoming more aware of their responsibilities. For example, on 20 November 1988, MAS Managing Director, Datuk Abdul Aziz Abdul Rahman, speaking on "the Role Of Companies in Society" to a group of businessmen mentioned that a company should acquire its corporate image in many ways, such as through advertising and sales, but its activities had a direct impact on the community. He also added that a corporation should not only have a mind of business but also a heart and soul that gives it a social conscience. Contributions from firms to society and community could come in different forms such as services, time and effort, apart from financial considerations. Corporations in Malaysia are now more aware of their social responsibilities in supporting

causes and issues which affect the community in which they operate. For example, in September 1988, the response from corporations towards the raising of funds for the underprivileged children of the world was overwhelming. Within a day, the target of \$2 million was easily attained!

Traditionally, accounting measurements have been made in terms of money. Whether an event should be recorded in accounting records depends primarily on whether it can be expressed in monetary terms. Consequently, some trivial items are recorded, but other items of considerable importance are ignored just because they are not easily quantifiable! However, this does not mean that the latter should not be included just because they are not easily quantifiable.

The more important issues are the nature and the method of disclosure so that the seven groups of users, identified by the Corporate Report Committee as the equity investors, the loan creditors, the employees, the analyst-advisers, the business contacts, the government and the public, can use the information disclosed to make informed judgements. It is debatable as to whether whatever available information or only the relevant information should be provided to the users. Making all information freely available to the users will put competitors in a better position to use such information to their own advantage. On the other hand, if only relevant information is to be provided, who should decide what is considered relevant. The Corporate Report Committee suggested that the following supplementary statements, for example, could be prepared:

1. A Statement of Value Added
2. An Employment Report
3. A Statement of Money Exchanges With The Government
4. A Statement of Transactions in Foreign Currency
5. A Statement of Future Prospects
6. A Statement of Corporate Objectives

In addition, the present financial statements do not provide any information about employees except for the wages and salaries shown in the profit and loss account. Long ago, Alfred Marshall stated "The most valuable of all capital is that invested in human beings." There is still very little sign of this being accepted by accountants. Employees are interested in the activities of the enterprise for a number of reasons, of which income is but one. Clearly, the employees are interested in sharing in the economic success of the firms. Therefore, financial statements are useful for future negotiations to get bonuses. They are also interested in job security. Hence, they are concerned with the long-term objectives of the organisation to remain in existence and to prosper. Employment by a firm is not simply a means of earning an income, it also means being part of a social group; it means acquiring an identity and a sense of belonging; they are also concerned with the conditions in which they are employed, the nature of management, the level of communication with the firm, job satisfaction and pride in the products. Such information like wage levels, employee skills, knowledge and job safety should be available whether quantitatively or qualitatively.

Attempts have been made to quantify the value of human resources in the firm. Information, being not easily quantifiable, does not justify its exclusion from the financial statements to allow the user access to sufficient information to make informed judgements and decisions.

Human resource accounting seeks to report and emphasise the importance of human resource – knowledgeable, trained and loyal employees – in a company's earning process and total assets. Such information can be valuable not only from the point of view of the employees but also that of the investors and the government. One of the most important, if not the most important, assets of an enterprise is the employees who can resort to force in making or breaking a firm especially when they are unionised. Employees form the backbone of an organisation. An organisation ceases to exist without them. The emergence of human resource accounting shows that this idea is gaining acceptance.

Being in its infancy, human resource accounting is fraught with many problems. It is theoretically impossible to show human capital on the balance sheet since it cannot be purchased or owned by the firm. Besides, the labour force may not have a service potential which extends beyond the current year. There are problems as to how human resources can be reasonably quantified, whether it be in one of the following methods or possibly some other methods:

1. Replacement Costs
2. Competitive Bidding Method
3. Capitalization of Salary
4. Economic Value Method
5. Return on Effort Employed
6. Behavioral Variables Method

Despite the problems, companies such as R.G. BARRY CORPORATION, TOUCHE ROSS & CO (Canada) and QUAKER OATS had attempted to show how human elements can be depicted in the Balance Sheet. Below is an example provided by Quaker Oats Company Annual Report 1973.

Assets	Liabilities
<ol style="list-style-type: none"> 1. Company expansion has provided approximately 10,000 new jobs since 1963 2. One of the first members of Plans for Progress (3-17-64) a Voluntary program to provide more job opportunities for minorities <p>Minority employment has grown from 6% in 1963 to 19% in 1972</p> <ol style="list-style-type: none"> 4. Women now constitute about 40% of total employment 	<ol style="list-style-type: none"> 1. Fluctuating employment levels still a problem at some plant locations 2. Need more upgrading of minority employees into higher labour grade jobs 3. Closing of Waterbury Work training center after Scorill investment of \$33,000 State and Federal grants to support it were terminated

If information is to be made available to the man in the street, financial statements would not be comprehensible to them. The information needs to be simplified and can be presented, for example, in the form of pie-charts about a particular product. In addition to the financial statements, simple statements, reports and diagrams could be included. A customer who does not understand the financial statements may understand the pie-chart. Included in the pie-chart are the profit and costs of making and selling the product. The customers, thus given some inkling of the profit generated, are able to figure out whether they have been undercharged/overcharged for the product in question. They can also tell precisely how much more they have to pay if they demand better service, superior products and punctual delivery.

Firms provide employment in the local community and for this reason the community is interested in the activities of local enterprise. At the same time, the local community would expect the firm to accept certain social responsibilities besides making profit. The community may face negative industrial outcomes such as waste disposal, atmosphere pollution and despoilation of countryside. Information such as costs borne by the firm to dispose waste would indicate whether the firm is doing its best for the community thereby fulfilling its responsibility. Accountancy therefore requires new measurement for defining social objectives and assessing the progress towards these objectives. The management team is responsible not only for the efficiency of operations as expressed in profitability (such as earnings per share) but also for what is done about social problems. Therefore, the measurements of performance derived from the financial statements are too narrow to reflect what many companies are trying to do.

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