



Cost and Budgeting

**Management of
Academic
Resources**

**Concept,
Importance
and Need**

**Strategies for
Quality
Improvement**

**Management of Student
Support System**

**Management of
Financial Resources**

2

“शिक्षा मानव को बन्धनों से मुक्त करती है और आज के युग में तो यह लोकतंत्र की भावना का आधार भी है। जन्म तथा अन्य कारणों से उत्पन्न जाति एवं वर्गगत विषमताओं को दूर करते हुए मनुष्य को इन सबसे ऊपर उठाती है।”

— इन्दिरा गांधी



“Education is a liberating force, and in our age it is also a democratising force, cutting across the barriers of caste and class, smoothing out inequalities imposed by birth and other circumstances.”

— Indira Gandhi



Block

2

MANAGEMENT OF FINANCIAL RESOURCES

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Expert Committee

Prof. Lokesh Koul Prof. Emeritus (Education) Himachal Pradesh University, Shimla, H.P.	Prof. S.L. Jena Former Director State Council of Educational Research and Training (SCERT) Bhubaneswar, Orissa	Prof. S.V.S. Choudhary Vice Chairman, NCTE Delhi
Prof. Snehaben Joshi Formerly with Deptt. of Educational Administration, Faculty of Education and Psychology. M.S. University of Baroda, Vadodara, Gujarat	Dr. Nayan Tara Faculty, Public Systems Indian Institute of Management Bangalore	Ms. Poonam Bhushan Lecturer (Selection Grade) Special Invitee SOE, IGNOU
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	Prof. S.K. Panda STRIDE, IGNOU	
	Prof. M.L. Koul Director, SOE, IGNOU	

Course Preparation Team

Course Contributors	Unit Design and Editing	Content Editing
Dr. Ashok Gaba Reader, SOVET IGNOU	Prof. Vibha Joshi SOE, IGNOU	Prof. M.B. Menon Deptt. of Edu UNRWA HQ(A), Jordon
Dr. Geetika Dutta Lecturer Army College of Education New Delhi	Proof Reading Mr. Trilokes De Consultant SOE, IGNOU	
Dr. S. Geetha Associate Professor NUEPA, Delhi		
Mr. Trilokes De Consultant SOE, IGNOU		

Production

Prof. M.L. Koul Director School of Education	Mr. S.S. Venkatachalam Assistant Registrar (Pub.)	M. Sumathy Nair S.O. (Pub.)
--	--	--------------------------------

October, 2009

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ISBN-978-81-266-4268-7

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Further information on Indira Gandhi National Open University courses may be obtained from the University's office at Maidan Garhi, New Delhi-110 068.

Printed and published on behalf of the Indira Gandhi National Open University, New Delhi by Director, School of Continuing Education, IGNOU.

Lasertypesetted at Graphic Printers, Mayur Vihar, Phase-I, Delhi-91.

Printed At :- Kalyan Enterprises ,215/5 Ambadker Gali Moujpur, Delhi -53

BLOCK 2 MANAGEMENT OF FINANCIAL RESOURCES

Introduction

Any organisation involved in any kind of economic activity has to maintain a systematic record of all the day-to-day transactions. The very basis of economic efficiency is based in identifying the financial resources we have at our disposal and to variety of uses we need to put them to. Accounting is that branch of knowledge which provided us ways and means of recordings of all the transactions pertaining to financial character in an organisation in a systematic and orderly manner. And so it is important to study and identify the different types of costs incurred by the institution and formed a sound fiscal plan or budget. It is important to mention that investment in education has been realised as an investment that bears high economic returns to the society, but it generally has took a longer gestation period. Similarly, huge resources are required for both quantitative expansion and qualitative improvement and also for the maintenance for the education system. Resource mobilization is one of them. It could be possible through internal and external resources. The present block contains four units covering different aspects on financial resources. So let us discuss briefly about all units:

Unit 6 of this block titled **Educational Finance: Meaning, Importance and Scope**. Here we have discussed meaning, scope and importance of educational finance. The different sections of the unit dealt with the different criteria for educational financing, resources mobilization and utilization, financing of school education versus tertiary education, pricing and subsidy of education, trends in expenditure among the different stages of education. We further preceded the discussion on these aspects which are closely related with the educational policies of a country.

Unit 7 dealt with **Costing and Budgeting**. It began with the concept, its classification, system, techniques and methods of costing, as well as the concept of budgeting and its types.

Unit 8 dealt with **Accounting and Auditing**. It describes the very concept of accounting and its importance in an educational institution. Subsequently discussion on the auditing, it's types and classification has been included. Preparation of an audit report is an important aspect of auditing, the points to be included in the audit report have been mentioned.

Last **unit i.e 9** of this block dealt with **Resource Mobilization in Education**. We discussed some major issues pertaining to the financing of education. Other sections of this unit discussed internal and external sources, governmental and non-governmental resources under internal resources. Simultaneously multilateral and bilateral resources have been discussed as a part of external resources also.

Block-1 Management of Curriculum

- Unit-1 Classroom Management (Instructional Management)
- Unit-2 Curriculum Transaction
- Unit-3 Management of Evaluation
- Unit-4 Management of Academic Resources
- Unit-5 Management of Curricular & Co-curricular Programmes & Activities

Block-2 Management of Financial Resources

- Unit-6 Educational Finance: Meaning, Importance and Scope**
- Unit-7 Cost and Budgeting**
- Unit-8 Accounting and Auditing**
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Block-3 Management of Human and Administrative Resources

- Unit-10 Management of Student Support System
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Block-4 Management of Infrastructure

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Block-5 Total Quality Management

- Unit-16 Quality Control, Quality Assurance and Indicators
- Unit-17 Tools of Management
- Unit-18 Strategies for Quality Improvement
- Unit-19 Role of different Agencies
- Unit-20 Quality Concerns and Issues for Research

UNIT 6 EDUCATIONAL FINANCE: MEANING, IMPORTANCE AND SCOPE

Structure

- 6.1 Introduction
- 6.2 Objectives
- 6.3 Educational Finance: Meaning
 - 6.3.1 Criteria for educational finance
- 6.4 Mobilisation of Physical and Financial Resources
- 6.5 Financing of School versus Tertiary Education
- 6.6 Sources of Educational Finance
 - 6.6.1 Contribution of government and household in educational financing
 - 6.6.2 Contribution of foreign aid in educational financing
 - 6.6.3 Cost effective model
- 6.7 Expenditure on Education
 - 6.7.1 Indian Expenditure on Education as a percentage of GNP
 - 6.7.2 Educational Expenditure by Level
- 6.8 Plan-wise Outlay on Education in India
- 6.9 Let Us Sum Up
- 6.10 Unit end Activities
- 6.11 References
- 6.12 Answers to Check Your Progress

6.1 INTRODUCTION

In this Unit an attempt has been made to describe meaning, scope and importance of educational finance. The various issues pertaining to financing for school versus tertiary education and subsidy to education have been discussed. The other sections of this unit dealt with different criteria for educational financing, resources mobilisation and utilisation, financing of school versus tertiary education, pricing and subsidy of education, trends in expenditure among the different stages of education. We preceded our discussion on these aspects which were closely related with the education policies of a country.

As we all know that educational finance deals with (a) policy issue, (b) planning methodology, techniques and administration procedures and management approaches in financing in education. So there are many sources for financing in education either government or private or public in the country. Actually government does not have any private sources of income. The government took resources or aid from others and subsidises the cost of our education. The main issue in financing in education is mobilisation of resources both - government and private resources, their allocation and utilisation in all levels of education.

Financial management is one of the importance aspect in any management. Similarly management of finances is equally important in educational context. The basic purpose

of an organisation is to produce and distribute knowledge as far as possible (service to the society). Finance is to business as well as educational venture what blood is to the human body. Thus it is the life blood of business or education. As we know that finance which brings together the various parts of an organisation and transformed that in various ways for smooth functioning of an institution and achieving the goal of an institution. Thus, finance has been recognised as the backbone of an institution.

6.2 OBJECTIVES

After going through this Unit, you should be able to:

- explain the meaning, scope and importance of educational finance;
- describe the adequacy, equity and efficiency of educational resources in education;
- describe the nature of the processes involved in the resource mobilisation and utilisation;
- explain the financing of school and tertiary education;
- explain sources and subsidy issues of education and contribution of fees, government grants and foreign aids in income;
- describe the process of educational planning in developing countries with special emphasis on India.

6.3 EDUCATIONAL FINANCE: MEANING

Finance is the science of the management of money and assets. It deals with resource allocation as well as resource management, acquisitions and investment. Presently, education is being provided through different modes such as formal, non-formal, distance and online (e-learning). For providing different levels of education through different modes a variety of resources are needed. In general, resources can be categorised into two broad types: human and non-human resources. Educational institutions run by money. It is also not necessary that all the problems of education can be solved by allocating money to them. But without money to secure the essential physical resources of education (buildings, equipment, materials) and human resources (teachers, administrators and custodians) would be not possible and eventually the organised educational system would collapse onto an empty centre (Coombs, 1985, p. 137). Therefore, money becomes very important for the survival of any system. So, let us define **educational finance**. It is the management of money and assets thereby physical and human resources are allocated for educational purpose. The next question would be how do we assess the systems of educational finance and what are the criteria for their assessment.

6.3.1 Criteria for Educational Finance

In this subsection let us try to understand the various criteria used for Educational Finance.

Benson (1987, p 423) defined three main criteria by which systems of educational finance are traditionally judged:

These are as follows:

- (i) whether the level of provision of educational services is *adequate*;

- (ii) whether the distribution of educational resources is *efficient*; and
- (iii) whether the distribution of educational resources is *equitable*.

These three criteria are interrelated. During the 1960s and the first half of the 1970s, *adequacy* was defined in terms of the percentage of gross national product devoted to education (the figure of eight percent was often deemed "adequate"), and in terms of the share of the central government's budget spent on education (20 percent was considered to be an appropriate figure). These kinds of measures are not thoroughly satisfactory because they sometimes ignore private education and educational revenues generated in provincial and local authorities. Their meaning was also confusing because they failed to address the question of the efficiency with which a given government run its educational programmes. The objectives by which adequacy of education is defined also require at least a minimum level of competence and commitment on the part of teachers. Required cost per capita will vary from country to country and even state to state, city to city, urban to rural areas and so on depending on the degree of efficiency with which the educational system is operated. Publicly financed institutions, whether at the school, technical institute or university level, ordinarily claim a certain degree of autonomy in managing their day to day affairs. In some instances, institutional views of educational policy may be contrary to the dictates of *efficiency*, as seen from a national perspective. Efficiency is always linked with achieving acceptable quality of the educational system within affordable resources.

There have been different views regarding *equity* issue of financing in education. Mostly central government seeks an arrangement, which is neither wholly centralized nor wholly decentralized. Complete centralization implies an excessive amount of bureaucratic delay in making decisions, and it also entails, probably, an incapacity to take proper account of changes in local needs and desired practices. Complete decentralization destroys the capacity of the central government to direct local authorities to meet long-range national needs for training personnel. It prevents a progressive administration from imposing higher standards of public morality on backward local authorities. Local authorities that have a pleasant climate in which the students are thoroughly middle class may be able to attract a teacher of given competence at a lower salary than an industrial suburb in a harsh climate may be required to pay. Using their estimates of local needs and local resources, the central government is likely to employ one of three main fiscal devices to link together central and local support for education.

The government has different procedures for educational finance:

First, government decides on the basis of per student cost.

Second, government share in the costs of a locally determined education budget and to share local budgets in such a position that any two local authorities that levy the same local school tax rate are provided with the same sum of money to spend per student. In this case, the percentage share of state money will be higher in a poor local authority than in a rich one.

Third main type of grant is the "**weighted-population grant**". This is the simplest arrangement of the three and the one that is the most flexible. One of the important considerations in the design of grants is the population features of the state(s), district and even in an institution. Population distribution, development index, proximity to development, geographical and educational status of the school are the common indicators that influence grants to an educational institution. For example, teachers working in schools located in difficult terrains get special incentives, scholarship/

freeship provisions for students from socially deprived population pockets and so on.

There is a need to evolve a financing mechanism for educational system. There is a comprehensive model or framework common to all the countries. This calls for comprehensive studies and data base on socio economic profile of the learners, and cost per student and the quality of the education which being provided by the educational institutions.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

1) What do you mean by educational finance?

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2) What are the criteria for assessing educational finance?

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3) What are the three procedures for the government finance ?

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6.4 MOBILISATION OF PHYSICAL AND FINANCIAL RESOURCES

In the previous section, you have studied about the meaning and criteria for educational finance. You have also studied about the requirements of physical and non-physical resources for the survival of any educational system. In this section, we shall discuss the non-human resources only. Non-human resources include both physical and financial resources.

In the developing countries, physical resources of capital nature for education are generally provided by the community. Land required for building educational institutions is often donated by individuals, religious bodies, trusts, industrialists, village panchayats or/and government. Some members of the community, who are financially well of, make liberal donations towards the construction of buildings and provision of other infrastructural facilities. Given the capacity, the extent of mobilisation of physical resources depends on the ability of the management of the institution and the community leaders to exploit these sources.

Financial resources, by themselves, do not make education provision possible until a country has acquired both the human and physical resources. The major role of financial resources is to mobilise human and physical resources and bring them together for providing education. Lack of financial resources adversely affects not only the maintenance of the existing system of education but also its development. The financial resources for education may be examined both from the point of view of expenditure and income (Bawa, 2001).

Very little research evidence is available on (a) the present pattern of utilisation of resources, and (b) the scope for effective utilisation. But researchers raised issues like pattern of allocation of financial resources at macro level to the education sector and whether optimum level of resources are allocated for education. The allocated budget funds need to be utilised for the purpose for which they were given. While re-appropriation may lead to the better utilisation in certain cases, it is not necessarily so in most cases, particularly when the original allocations were made after careful examination of the needs of the system. It is also necessary to estimate normal unit costs, and also the 'effective' costs, measuring the real effectiveness of the system, while analysing **cost size relationship**. The utilisation of resources in education is a function of several inter-related factors that lie both within the education system, and outside. Factors including are institutional factors, behavioural aspects, managerial aspects, existing norms, rules and procedures, etc., some of which may not be quantifiable. But all are important. One has carefully analysed the relative effectiveness of various inputs, before suggesting reallocation.

There is a need for research in the area of relative effectiveness of hardware (e.g. buildings) versus software (e.g. books). There may be paradoxical situation, such as one characterised by very low level of resources and complete utilisation, in contrast to a situation characterised by large amount of resources and under utilisation. Lack of financial resources adversely affects not only the maintenance of the existing educational system but also its growth in the country.

Check Your Progress

Note : a) Space is given below for writing your answer.

b) Check your answer with those given at the end of this unit.

4) Explain effective type of utilisation with example

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6.5 FINANCING OF SCHOOL VERSUS TERTIARY EDUCATION

In the previous sections, we apprise you about the criteria for educational finance and resource mobilisation and utilisation in educational system. In this section, we shall study about financing of school versus tertiary education.

How do you balance between financing different sectors of education? There is always debate over financing of school education vis a vis tertiary education. Each country has its own educational priorities, system of government finance, political

mechanisms for making decisions and administrative structures for implementing them. Schools' finance represents one of the major dimensions of these structures and processes, and such financial decisions must be made along with broader policy decisions in education and in the larger society. In a sense, each educational decision has implications for ascertaining how resources will be obtained and allocated. By reviewing a number of different decision areas in education, it is possible to see their consequences for school finance (Levin, 1987).

On the other hand, tertiary education is an important element in national economic performance and a major determinant of a person's life chances. But it is costly, and faces competing imperatives for public spending. Its financing is therefore, important and immensely sensitive politically. Despite the problems, widespread agreement exists on two core objectives: *strengthening quality and diversity*, both for their own sake and for reasons of national economic performance; and improving access, again for both efficiency and equity reasons. If it is not possible to rely completely on public funding, it is necessary to bring in private finance—but in ways that do not deter students from poor backgrounds. There is also a different opinion emerging among economists that tertiary education is a right and should therefore be financed from taxation. However, the fact that something is regarded as a right does not mean that it should be tax-financed. For example, access to food and education is a basic right, yet nobody argues that it is wrong to charge for it. The moral imperative is not about instruments (for example, prices) but about outcomes, that is, that a gifted or talented children should be able to go to the best school or university irrespective of his / her financial circumstances. The historical record shows that tax finance has done little to widen access, while, as noted, tax finance is deeply regressive. If it is unfair to ask graduates to pay more for the cost of higher education, it is even unfair to ask non-graduate taxpayers to do so.

It may be noted here that in developing countries like India, there exists a complex mechanism for providing financial resources at meeting expenditure at different levels as presented in Table 6.1. This will give you an overview about percentage of the total educational expenditure at different levels.

Table 6.1: Expenditure on Education in the Five Year Plans (In Percentage)

Five Year Plan	Elementary	Adult	Secondary	Higher	Technical	Total	% of Total Plan Outlay
1 st	56	3	13	9	13	100	7.86
2 nd	35	1	19	18	18	100	3.83
3 rd	34	0.3	18	15	21	100	6.87
4 th	30	1	18	25	13	100	5.04
5 th	35	4	17	22	12	100	5.04
6 th	30	3	25	18	11	100	3.27
7 th	34	6	22	14	12	100	3.50
8 th	42	8	16	7	13	100	4.90
9 th	51	2	18	8	9	100	6.20

Source: Tilak, J.B.G. (2003) Public expenditure in India, in Tilak J.B.G. (Eds). Financing Education in India, Current Issues and Changing Perspectives, New Delhi: NIEPA & Ravi Books, p. 24.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

5) Why is financing politically sensitive?

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6) Based on efficiency and equity reasons what are the two core objectives of tertiary education?

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7) What are the three procedural for the government finance ?

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6.6 SOURCES OF EDUCATIONAL FINANCE

Who will invest in education and why? Those invest in education from where they will get money? Let us examine a case as an illustration here to reply to these questions. You will find that your education involved a cost. Cost could be both private and public and it has yielded stream of benefits both to private and public. First, we present you the costs in education here. There were some private costs, which were borne by your family. They spent their private time and money out of their pockets to pay for part of your education. You too spent time; time which has an opportunity cost. You could have been doing some job and adding to your family income instead of going to school. That needs to be added to the account for the private costs. Apart from the private costs, there were public costs. Your family did not pay full price for your education. The government paid part of your fee. The government did not actually pay since the government does not have a private source of income. The government took resources from others and subsidized the cost of your education. In other words, the general public paid for part of your education and you think the major part of the cost was paid for by the public. You, and indirectly your family, benefited from this *subsidy*, which was achieved through a transfer of resources (taxes). Adding up the private and public components of the costs gives us the "social" cost.

Like the costs, the benefits can also be distributed as private and public, and the sum of the two is the social benefits. The private benefits are easy to account for. Had you not acquired the skills during all those years in school, you would not have been able to earn the amount you earn today. The returns to the private investment in your education, thus, is not just positive but incredibly positive. What about the

public benefits? Because of your education, you are a more productive worker and hence create more stuff than you would have had you not been educated. Though it is hard to quantify, you add some amount of wealth to society. It is trivially true that you must add more wealth to the society than what you paid as salary. This is so because what you produce must be worth more to your employer than your salary. The difference between your salary and the total wealth you produce is what is the public benefits of your existence. Add the private and public benefits, and you arrive at the social benefits.

If the social benefits exceed the social costs, then society is better off investing. And, if private benefits exceed private costs, then a private person is better off investing. In your case, both conditions exist. Society is better off for having subsidized your education and your family is better off for having invested a little in your education. But those who have the money to invest in education are privileged enough to get subsidized education, and are reaping the benefits of that education. But unlike you, the poor are credit constrained. They too would privately benefit from investing in education, and society too will benefit from having them being educated, but as it happens, the poor cannot afford to make that investment. Therefore, government grants funds for poor students.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

8) What is social benefit?

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9) What is opportunity cost?

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10) When is society better off in investing?

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11) When is a person better off in investing?

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6.6.1 Contribution of Government and Household in Educational Financing

Government meets the institutional costs of education to a large extent. Elementary –primary and middle (upper primary) education is almost fully financed by the government- Central, State and Local bodies. Generally, government – Central, State and Local bodies –meet 99 per cent of the total recurring expenditure at primary level and 96 per cent at upper primary level.

Generally high levels of household investment in education are favoured on the following three main grounds:

- Government does not have adequate resources to finance education and hence households have to necessarily finance their education at least partly;
- It is believed by some that household expenditure, including specifically fees, would improve efficiency in the system, by making the children more serious with studies, and
- Household expenditure reflect both ability to pay and willingness to pay for education. It is argued that the ability and willingness to pay need to be fully exploited.

At the same time, there are strong arguments against household expenditures. The phenomenon of household expenditure, particularly on lower levels of education is against the letter and spirit of free and compulsory education in many countries, as enshrined, for example, in the Constitution of India, and in several UN declarations, including Convention of the Rights of the Children. Students in primary schools, who were enrolled even in government schools, were found to be paying fees of various kinds, including tuition fee, apart from incurring huge expenditure on various other items. Fees are found to form a major component of expenditure of the households on their children's schooling. Other significant determinants of household expenditures are the average size of the household, schooling levels of the population in the state, poverty, government expenditure on education and the size of the private school sector in a state. Constraints on availability of data on the one hand, and multi-co-linearity between the few selected variables are the two major weaknesses of the exercise attempted in this context (Tilak, 2003). The Union Government of India passed a Free and Compulsory Education Bill in order to make the 86th amendment to the Constitution that has made elementary education a fundamental right, statutorily enforceable. Tilak (2004, p.619) remarks on this bill "It does not discourage the growth of the fee-charging private school system. In fact, in several ways, through several clauses, the bill seems to be encouraging dual system of elementary education –public education system (of poor quality) for the poor, and fee charging private education (of better quality) for those who can afford."

On the other hand, institutions that generate revenues on their own were also provided with added incentives, in terms of grants, etc. As a result of all these policy directives, there was a race among many institutions to generate resources on their own, through

- substantial and erratic increases in fees and introduction of fees for items which were earlier provided free-such as application fees, fees for marked assignments, extra fee for consolidated mark statements, fees for authentication of transcripts and others;
- introduction of self-financing courses, and
- consultancy, sale of services, etc.

Cost recovery has been the exhortation and it largely refers to recovery from students' through fees and other charges. Those who are critical of the proposed cuts in fees levels have also argued in this context that the state should subsidise only primary education, and should not subsidise higher education. Neither empirical evidence from other countries nor theory supports such view. High levels of fees, and reduction in state subsidies lead to privatisation of higher education. Cut in fee levels will lead to increase in enrolment of students from lower economic background. This in turn would lead to fall in quality and standards of higher education, this equating lower economic background to low quality, quite ignoring that distribution of merits is not so skewed in favour of the rich (Tilak, 2004b, p.871).

A discriminatory fee structure implies that fee will be charged according to the paying capacity of the student, the fee to be levied based on the cost of providing education for each faculty or subjects on the one hand and paying capacity of individual students on the other. Needless to add, those belonging to the highest socio-economic households will pay the most, close to the full pricing of education. Students from the lowest social and economic households will pay the least which indirectly helps target subsidies in favour of the poor. One can argue that discriminatory pricing may lead to an increased income for higher education without adversely affecting equity considerations in educational provisions. In this sense, a discriminatory fee structure will reduce the perverse effects of the existing public subsidy system (Varghese, 1987).

However, in case of higher education in the country as a whole, government subsidies are about three-fourths of the total recurring expenditure. Student fees and endowments and others meet the rest more or less in equal proportions. But in the recent years, given the changing economic and educational policies, the proportion seems to be rapidly increasing to significant levels in many Universities.

It is interesting to note that even when there was a decline in public funding for higher education, the non-professional courses were more adversely affected than the professional ones. The 1980s was a period of economic crisis in many developing countries. During this period many countries resorted to extensive external funding, primarily through the structural adjustment programmes. Studies have shown that countries which received structural adjustment loans showed declining public expenditure on education. It was primarily due to the fact that structural adjustment necessitated a redefinition of the role of government and envisaged a reduced government intervention in all sectors, including education.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

12) Why do household investments favoured?

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13) What are the arguments put forward against household investment?

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- 14) How does Union Government of India guarantees elementary education as a fundamental right?

6.6.2 Contribution of Foreign Aid in Educational Financing

Foreign aid is one important source of finances for education in several developing countries. Its importance gets enhanced in developing countries like India where public budgets for education become very tight with the adoption of structural adjustment policies. Currently, a large number of primary education projects have been in progress under the District Primary Education Programme (later named Sarva Shiksha Abhiyan), from assistance by several international agencies, such as the World Bank, the Swedish International Development Agency, the UNICEF, the Overseas Development Administration (ODA), the European Economic Community, etc. Thus the external aid is both bilateral flowing from countries, and multi-lateral flowing from international- UN and other organizations.

The effect of aid on education in India is yet to be seen. But high expectations are being created on the contribution of foreign aid for primary education, particularly with the launching of the social safety net programmes with the help of assistance from the World Bank, that are being initiated to reduce the adverse effects of structural adjustment policies that are being adopted. There are very few studies on the role of foreign aid for education in India (Tilak, 2003).

In US, the country with the biggest system of higher education and the country where the high-priests of privatisation call the shots, 80 percent of the higher education sector is sustained by government funding. The rest of the money comes from endowments and only some bit of the resources is generated by the institutions themselves. And how is expenditure to be controlled in a university? There is the practice to cut expenditure on salaries by appointing ad hoc teachers to whom no dearness, housing, city compensatory, travel, medical allowances are paid. Nor is any contribution to the provident fund or pension fund of such teachers deemed necessary. Similarly, to cut the costs of building campuses, universities have authorised study centres to dispense education for their degrees, especially, in computer software. All this has given higher education the nick name of 'hire education' (Tilak, 2004b).

In India analysis of recurring (non-plan) expenditure by level (i.e. from primary schooling to higher education) shows that 94.5 percent of the expenditure on school education was met by government sources. The corresponding proportion for higher education (in 1986-87) was 76 percent and 'fees' and 'endowments' accounted for the rest (i.e. 12 percent each: These are presented in Table 6.2. Privatization of higher education which was encouraged as a matter of government policy during 1990s, and the impact of which is not fully reflected in the data presented for 1992-93 in Table 6.2, is expected to increase the share of the component to a much higher level.

Table 6.2: Sources of funds (recurring) for education in India: 1992-93 (%)

Level/Source	Government	Local bodies	Fees	Endowments etc.	Total
Primary	91.1	7.5	0.0	1.4	100.0
Middle	88.6	8.0	0.0	3.3	100.0
Secondary	93.2	3.0	2.9	1.0	100.0
Higher secondary	84.4	3.6	10.2	1.8	100.0
Intermediate	18.2	0.8	58.8	22.2	100.0
Total school sector	89.5	5.0	2.9	2.6	100.0
Higher education (1986-87)	75.9	0.0	12.6	11.5	100.0

Source: Tilak (2004a)

A commonly suggested cost recovery method, therefore, is to increase students fees. The share of fees in the total expenditure in higher education has declined over time (Table 6.3). This has happened because fees for courses in higher education was kept constant for a long time even though the cost of providing education increased manifolds. In the Indian context, the following alternative ways of increasing the fees have been suggested:

- (i) a uniform increase for graduate and post-graduate courses;
- (ii) increasing the fees based on the cost of provision of courses; and
- (iii) giving autonomy to colleges for deciding on the fees to be charged for courses offered, and others (Tilak, 2004).

In most colleges and universities over 90 percent of the expenditure goes towards paying salaries of teachers and staff. Therefore, it is not surprising that many dual mode universities have been resorting to distance education.

Table 6.3: Funding for Higher Education by Source (percent)

Year/Source	Government	Local bodies	Fees	Others	Total
1950-51	49.1	0.3	36.8	13.8	100.0
1960-61	53.1	0.4	34.8	11.7	100.0
1970-71	60.4	0.5	25.5	13.5	100.0
1980-81	72.0	0.8	17.4	10.8	100.0
1985-86	79.7	1.4	14.4	4.5	100.0
1986-87	75.9	0.0	12.6	11.5*	100.0

* includes local bodies.

Source: Tilak (2004a)

6.6.3 Cost Effective Model

For decreasing cost in education, most of the developing countries adopted cost effective models for delivery education i.e. Open and Distance Learning (ODL) System. Open universities and open schools have been established both at the national and state levels in India. ODL system reduces recurring expenditure on account of salaries and non-recurring expenditure on account of institutional arrangements for imparting education. Therefore, one of the strategies adopted in India to meet the increasing demand for higher education is through the open university

system and correspondence courses. Enrolment in higher education in the non-institutionalised sector (open universities and correspondence courses) has increased by 20% in India since last couple of years. It needs to be noted that this sector does not necessarily cater to the age-group which normally attends courses in universities and colleges. It is now well known that in face to face, about 90% funding come from government sources where as, contribution of ODL system is almost nil in most of the ODL institutions in India. We shall discuss in detail of this issue in the forthcoming sections.

Check Your Progress

Note : a) Space is given below for writing your answer.

b) Check your answer with those given at the end of this unit.

15) Why is ODL considered cost-effective mode?

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6.7 EXPENDITURE ON EDUCATION

So far you might have understood the criteria for educational finance presented in the previous section. It describes that the total allocation to education as a percentage of Gross Domestic Product (GDP) or Gross National Product (GNP) is an important indicator for *adequacy* in financing of education. There is also the view that 'normally', expenditure on education should grow at double the rate of economic growth in early stages of educational development (Tilak, 2006).

The pattern of institutional funding is reflective of the state policy on education. The government/public expenditure on education in selected developing countries (Table 6.4) indicates that, as percentage of GDP, these countries spend much less on education generally, though countries like Thailand and Myanmar spent as high as 31% and 18% respectively of the total government expenditure on education. This, however, is not reflective of their expenditure on higher education.

Table 6.4: Public Expenditure on Education (2000-01)

Country	As % of GDP	As % of total government expenditure
Myanmar	1.4	18.1
Indonesia	1.5	9.6
Pakistan	1.8	7.8
Bangladesh	2.5	15.7
Sri Lanka	3.1	-
Philippines	3.5	-
India	4.1	12.7
Thailand	5.4	31.0
Malaysia	6.2	-

Source: UNESCO (2003)

Contrary to what is noted above, in some of the countries, federal and provincial governments have been supporting higher education considerably. In Denmark, Netherlands, Canada, India, and USA governments provided funding support to campus-based higher education to the tune of 99%, 98%, 90%, 89%, and 78% respectively. These World Bank data further suggest that, in countries like Norway, France, Australia, Germany, Indonesia, Kenya, and U.K., government finance for higher education was 90%, 89.5%, 88%, 68.5%, 62.8%, 62.2%, and 55% respectively (World Bank, 1995). However, both the OECD (Organization for Economic Co-operation and Development) countries (which include largely the developed countries including Canada and USA) and the WEI (World Education Indicator) countries (which include developing countries and Russia) spent almost similar amount as percent of GDP on tertiary education (i.e. 1.4%), and some of the WEI countries like Jamaica and Malaysia spent more than the OECD countries (UNESCO, 2005a). Due to the transition of higher education from an elite system to a mass system during the last few decades in all of these countries, the governments are finding it difficult to support further expansion of higher education and the offering of higher education to large masses has led to the proposal of cost recovery, especially from students. Some of the countries, however, have increased percent GDP expenditure for higher education to meet the growing demand. It is therefore not surprising that most of them have resorted to distance and allied forms of delivery of education and training (Panda and Gaba, 2008).

Check Your Progress

Note : a) Space is given below for writing your answer.

b) Check your answer with those given at the end of this unit.

- 16) How does the OECD countries compare with WEI countries in spending for higher education?

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6.7.1 Indian Expenditure on Education as a Percentage of GNP

The Education Commission of 1964-66, the most comprehensive education policy document so far, recommended that the government should endeavour to progressively increase its expenditure on education to reach the level of 6 % of national income (i.e., GNP) over a twenty year time frame. The federal government of today is seriously considering doing so. Trends show (Table 6.5) that the expenditure on education in India increased two-folds over the period 1966-86 (from 1.8 % of GNP in 1965-66 to 3.7 % in 1985-86). The highest that it reached in the successive years was 4.4 % in 2000-01, whereupon there is a visible declining trend. The decade over growth rate in average per capita real expenditure on education suggests that while there was an increase from 5.7 percent in 1970s to 6.4 percent in 1980s, it declined to 4.1 percent during 1990s. This is largely attributed to the efforts of the government to withdraw from the education sector (particularly the higher education sector) during 1990s. It has been pointed out that in countries like India and Chile expenditure has increased faster than the increase in student enrolment. The reverse is the case for countries like Brazil and Philippines (UNESCO, 2005).

**Table 6.5: Indian expenditure on education as a percentage of GNP:
1951-2005**

Year	Expenditure as a percent of GNP
1951-52	0.67
1965-66	1.82
1985-86	3.71
1989-90	4.21
1999-2000	4.30
2000-01	4.40
2001-02	3.90
2002-03	3.83
2003-04 (RE)	3.81
2004-05 (BE)	3.54

Source: Tilak (2006)

RE: Revised estimates; BE: budget estimates

6.7.2 Educational Expenditure by Level

The analysis of budgeted expenditure shows that elementary education accounts for around 45 percent of total expenditure on education by the government (Table 6.6). There is a slight increase in from 1995-96 onwards, which is at the cost of secondary and technical education.

Table 6.6: Budgetary Expenditure on Education (per cent)

Year	Elementary	Secondary	Technical	Higher	Total
1990-91	46.3	32.2	4.4	13.4	100.0
1991-92	46.3	33.0	4.3	13.0	100.0
1992-93	45.2	34.3	4.3	12.9	100.0
1993-94	46.2	33.2	4.3	13.3	100.0
1994-95	46.4	33.2	4.4	12.9	100.0
1995-96	48.3	32.8	4.1	12.3	100.0
1996-97	49.1	32.3	4.0	11.8	100.0
1997-98	49.6	32.3	3.9	11.8	100.0
1998-99	49.0	32.6	4.1	11.9	100.0
1999-00	48.1	30.9	3.9	12.7	100.0
2000-01	48.9	30.1	3.9	14.8	100.0

Source: Tilak (2004c), p-347

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

17) Why did public expenditure in education declined during the nineties?

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18) Which level of education got largest expenditure by Government of India?

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6.8 PLAN-WISE OUTLAY ON EDUCATION IN INDIA

From the First-Five Year plan, launched in 1951, educational planning has continued to be a part and parcel of every Five Year Plan of India. Planning Commission consolidates the Central Plan prepared by the MHRD and State Plans prepared by various state's Governments and proposes an integrated national plan for educational development.

The main priorities in the First-Five-Year Plan were:

- (i) to make available, in various fields, personnel of suitable calibre;
- (ii) to satisfy the cultural needs of the people;
- (iii) to stimulate the growth of facilities that would help in the development of creative abilities, and
- (iv) to increase the capacity for enjoyment and to develop the spirit of critical appreciation of arts, literature and other creative activities.

In the First Five Year Plan, education was allocated 1,690 million rupees, but only 1,530 million was actually spent. This was 7.86% of the total plan outlay. Two facts that are indicative of the approach followed for educational investment in the First Five Year Plan are as follows:

- within the general category of education, elementary education was given the highest priority, followed by secondary and university education. The weightage given to secondary and university education put together was a little above one-third of that given to the elementary education.
- Second, the priority given to technical education was a little more than one-sixth of that given to general education.

In the Second Five Year Plan, a sum of Rs.3,070 million rupees was allocated to education. Out of this amount, Rs.2,730 million rupees was actually spent which was 3.83% of the total plan outlay. Few changes in priorities, as compared to the First Plan, are given in 2nd plan. They are as follows:

- First, in the general category, the weightage given to elementary education was drastically reduced (21%) and this was diverted to the university sector (9% more) and the secondary education sector (6% more).
- Second, there was an increasing trend in the priority given to technical education (5% more than the First Plan).

In the Third Five Year Plan, education was provided Rs.5,600 million. The actual expenditure, however, was Rs.5,890 million which was 6.87% of the total Plan outlay. So far as weightage to various levels and types of education were concerned, there were minor reductions in the expenditure of all the levels of general education, whereas more importance was given to the spread of technical education.

In the Fourth Five Year Plan, an amount of Rs.8,220 million was allotted to education, out of which only Rs.7,860 millions were spent (i.e.5.04% of the total Plan outlay). You would notice that, in comparison to the Third Five Year Plan, in the general category of education, weightage given to university education increased from 15% to 25%. Another important point to highlight here is the low priority given to technical education (the weightage was lower than even that of the Second Five Year Plan). So it can be concluded that there was expansion of general higher education at the cost of technical education.

The Fifth Five Year Plan (1974-79) aimed at ensuring equality of opportunity as part of the overall planning strategy to provide social justice, and establish closer links between the pattern of education on the one hand and socio-economic development on the other hand. The emphasis shifted from university education to the expansion of elementary education. The reduction of weightage for technical education was 1%. Moreover, there was a slight increase in the weightage given to general education. In the Fifth Five Year Plan, the total allocated budget for the educational sector was Rs.12,850 million (i.e., 3.27% of the total plan out lay), out of which only Rs.9,120 million (i.e., 2.31%) were finally spent.

In the Sixth Five Year Plan, the total outlay for education was Rs.25,237 million, constituting 2.60% of the total Plan outlay. The actual expenditure for the entire Plan period amounted to Rs.29,430 million (i.e., 2.70% of the total outlay). Though, there was reduction in the weightage given to technical education and university education, and increasing priority attached to elementary education, the total weightage given to the total general education showed an increasing trend. This difference was due to more emphasis given to general education (an increase of 2.20%) which included adult and non-formal education.

The Seventh Five Year Plan allocated Rs.63,826 million to education, i.e. 3.55% of the total plan outlay; while the actual expenditure came to be Rs.85,000 million (i.e., 3.50%). Similarly, during the Eighth and Ninth Five Year Plans the total actual expenditure was 2,12,120 million (4.90% of the total plan outlay) and Rs. 53520 million (6.20% of the total plan outlay) respectively. There was a special emphasize given to elementary and secondary education at the cost of tertiary education.

Check Your Progress

Note : a) Space is given below for writing your answer.

b) Check your answer with those given at the end of this unit.

19) Mention any two priorities areas given to various levels and types of education in first fifth five years plan in India

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6.9 LET US SUM UP

In this unit, you have learnt about the meaning and the nature of criteria for educational finance, resource mobilisation and utilisation, financing of school versus tertiary education, sources of educational finance in general and in India in particular, expenditure on education in India, Plan-wise outlay on education in the country.

The financial resources depend upon both human and physical resources for further utilisation and compare both income and expenditure. Additional resources can be generated by the government levying taxes on the private firms, and increasing the fees for various courses at the higher education stage. Besides, the government spending on education can be reduced by measures, such as privatisation, providing education through open and distance learning and adopting cost effective methods.

There is a need to change the approach to funding education. It has to be recognized that it is a public good, a merit good, a basic human right and an important instrument of socio-economic equity, besides being an important investment in human development as a whole, with intrinsic value of its own.

6.10 UNIT END ACTIVITIES

Select any educational institution. Study the financial authorities, scope and analyse. Write a report highlighting the positive and limitations of their financial estimates of an academic session.

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6.12 ANSWERS TO CHECK YOUR PROGRESS

- 1) Ref. section 6.3
- 2)
 - a) Whether the level of provision of educational service is adequate
 - b) whether the distribution of educational resources is efficient, and
 - c) Whether the distribution of educational resources is equitable
- 3) Ref. section 6.1 & 6.3
- 4) Ref. section 6.4
- 5) Ref. section 6.5
- 6)
 - a) Strengthening, and
 - b) Diversity
- 7) Ref. section 6.5
- 8) Ref. section 6.6
- 9) Ref. section 6.6
- 10) Ref. section 6.6

- 11) Ref. section 6.6
- 12) The household investments in education are favoured on the following three main grounds :
 - i) Government does not have adequate resources to finance education and hence households have to necessarily finance their education at least partly;
 - ii) It is believed by some that household expenditure, including specifically fees, would improve efficiency in the system, by making the children more serious with studies, and
 - iii) Household expenditure reflect both ability to pay and willingness to pay for education. It is argued that the ability and willingness to pay need to be fully exploited.
- 13) Ref. subsection 6.6.1
- 14) Ref. subsection 6.6.1
- 15) Ref. subsection 6.6.3
- 16) Ref. section 6.7
- 17) Ref. subsection 6.7.1 & 6.7.2
- 18) Ref. subsection 6.7.2
- 19) The main priorities in the First-Five-Year Plan were:
 - to make available, in various fields, personnel of suitable calibre;
 - to satisfy the cultural needs of the people;
 - to stimulate the growth of facilities that would help in the development of creative abilities, and
 - to increase the capacity for enjoyment and to develop the spirit of critical appreciation of arts, literature and other creative activities.

UNIT 7 COST AND BUDGETING

Structure

- 7.1 Introduction
- 7.2 Objectives
- 7.3 Concept and need for Costing and Budgeting
- 7.4 Costing
- 7.5 Classification of Cost
 - 7.5.1 On the Basis of Variability
 - 7.5.2 On the Basis of Controllability
 - 7.5.3 On the Basis of Relevance
 - 7.5.4 On the Basis of Normality
 - 7.5.5 Other costs concept of Decision making
- 7.6 Some Basic Concepts
- 7.7 System of Costing
- 7.8 Techniques of Costing
- 7.9 Methods of Costing
- 7.10 Budgeting
- 7.11 Why Do We Need Budgets?
- 7.12 Types of Budgets
 - 7.12.1 Master Budgets
 - 7.12.2 Departmental Budgets
 - 7.12.3 Fixed Budgets
 - 7.12.4 Flexible Budgets
- 7.13 Budgetary Control
- 7.14 Let Us Sum Up
- 7.15 Unit End Activities
- 7.16 References
- 7.17 Answers to Check Your Progress

7.1 INTRODUCTION

Any organization (whether for profit or not-for-profit) strives to attain economic efficiency. Economic efficiency basically refers to putting our limited financial resources (which have multiple uses) to their utmost utility so that we can maximize our satisfaction. The very basis of economic efficiency lies in identifying what financial resources do we have at our disposal and to what uses we need to put them to. These resources have to be used very judiciously as most of the expenses that we incur today have far reaching consequences. Therefore, it is very important for a school or college head to study and identify the different types of costs incurred or to be incurred by the institution and form a sound fiscal plan or budget. Such planning requires estimating future costs and expenses, prioritization of needs and performing cost-benefit analysis and then taking decisions. This in turn will enable the

institution to provide better educational services to the students and ensure economic and educational efficiency. In the following pages we will be dealing with the Costing and Budgeting process.

7.2 OBJECTIVES

After the completion of this unit, the learners will be able to:

- define and differentiate the terms cost and costing
- classify the costs into its various types
- differentiate between fixed costs and variable costs and discuss their impact on decision-making
- identify the costs relating to any institution as controllable and non-controllable costs
- discuss the impact of normal and abnormal costs on an institution
- take into account the opportunity cost of various alternatives pertaining to a problem situation
- make sound decisions taking into account the replacement and differential costs
- explain Cost Unit, Cost Centre and Cost Driver
- elaborate upon the two basic systems of costing
- discuss the relevance of different techniques of costing for an institution
- discuss in detail the method of operating costing for educational institutions
- prepare Cost-Sheet for any educational institution given relevant data
- explain the concept of Budgeting
- elaborate upon the importance of preparing Budgets by an educational institution
- discuss the different types of Budgets
- discuss the role and importance of Budgetary Control in an educational institution

7.3 CONCEPT AND NEED FOR COSTING AND BUDGETING

Case:

ABC Educational Trust has been running a couple of schools for the past 15 years. In this span of time their schools have earned a good brand name for themselves. But they were confronted with number of queries like:

- How to keep a tab on the costs of the institution?
- How to manage funds effectively?
- How to decide which ventures to indulge into and what should be level of operations?
- On what basis should these decisions be taken and by whom?
- Also how can different senior people be involved in the decision-making process so that the employee morale is high?

- How can we systematically arrange for funds for the more viable ventures?
- Also how can we come to know if the institutions are actually doing well or not?

In order to get an answer to these fundamental questions, they consulted a professional accountant and the accountant advised them to study some details about costing and budgeting in order to find answers to their questions. This unit is an endeavor to make you familiar with the most basic concepts of costing and budgeting so as to make them capable of taking sound decisions.

7.4 COSTING

According to the **Chartered Institute of Management Accountant (CIMA)**, **Costing** is the technique and process of ascertaining costs. It lays down basic principles to be followed for ascertaining the cost of products, jobs, processes and services. The process of costing is very dynamic and keeps on changing from time to time and from industry to industry. The application of techniques helps the accountant and management in deciding how to reduce and control various costs.

Now, Cost as we all know, refers to the amount of resources spent for producing a product or for rendering a service. The resources may be **tangible** (eg. material, equipment, transport etc.) or **intangible** (eg. Wages, salaries, rent, electricity charges, etc.). The cost may be a **fixed** amount for a lease period or duration (eg. rent of the building) or **variable** (eg. stationary, electricity, petrol etc). We will study about the different types of costs in following sections.

- **Cost and Expense Distinguished:** Expense for a year is the amount charged to the final accounts for that particular year. When the economic benefit of an outflow of resources is received and matched against revenue, it becomes an expense. Whereas, 'Cost' is the amount of expenditure (actual or notional) incurred on, or rather attributable to, a given thing. It refers to the resources spent for producing a product or rendering a service. These resources may be tangible or intangible. Payment for these resources may have been made in the past, present or to be made in future. Computation of cost, to a large extent, depends on (a) the type of industry or service and (b) the context in which it is used. Some amount of volunteers render to the institution and benefit given in exchange.

7.5 CLASSIFICATION OF COST

One of the most important inputs in managerial decision-making is cost. All major decision-making includes a detailed analysis of costs involved. Therefore it becomes imperative for managers/ principals/heads of educational institutions to have a profound knowledge on different types of costs and their impact on the overall functioning of the institution. The concept of cost is divided into the following categories:

7.5.1 On the Basis of Variability

This criterion deals with the change in the level of operation of an institution; whether the costs vary or not. There are four types of costs on the basis of variability as discussed below-

- **Fixed Costs-** Costs which do not change with the increase or decrease in the level of operation are **Fixed Costs**. The examples include rent of the institutional

premises, salary of permanent employees, depreciation on fixed assets etc. Following figure 7.1 illustrates the fixed cost:

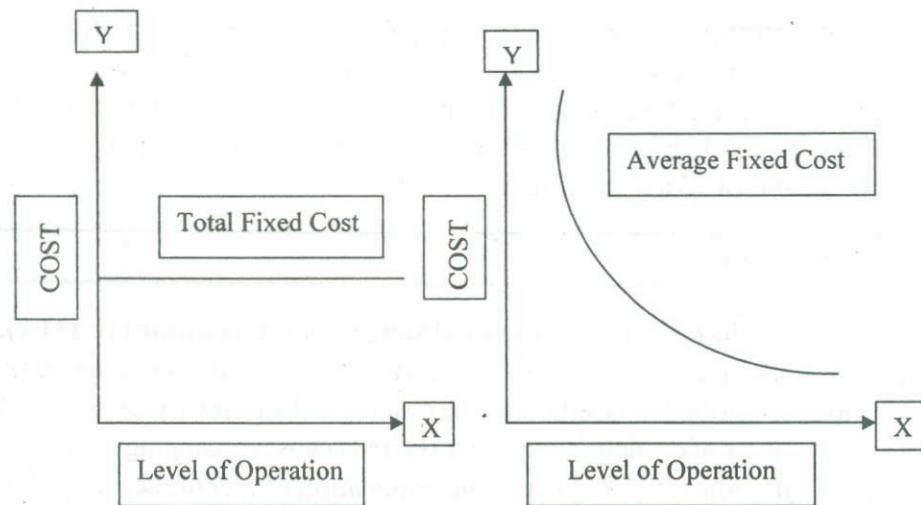


Figure 7.1 : Fixed Cost

From the above figure it is clear that the total amount of fixed cost remains the same but as the level of operation increases, the cost per unit decreases and vice-versa. Clue: In figure 7.1 (a) the straight line parallel to x-axis shows that as the level of operation increases fixed cost remains same. For example expenditure on land rent, managerial salary remains constant in short run even if we increase the production etc. . For example expenditure on land rent, managerial salary remains constant even if we increase the production. So if in a school the salary of the manager is Rs. 20,000 p.m., for the total strength of 2000 students, if the strength is raised to 3000 students, then also the salary is going to remain the same. In figure (B), a curve sloping downwards shows that as we increase the production, cost per unit decreases. Taking the same example, per student cost of manager's salary is Rs. 10. but if we increase the strength to 3000 students it will come down to Rs. 6.67 and if the strength is 4000 then it will be Rs. 5 per student. So we can see that per unit cost keeps on decreasing if we keep on increasing the number of cost units.

You can take an example from government sector also. Like plan and non plan expenditure is there. In figure 7.1, a curve sloping downwards shows that as we increase the production, cost per unit decreases. Let us take an example. If we are producing 100 books per unit cost is 1,00,000 and if production is increased to 200 books, per unit cost is 50,000 and if 300 books then 33,333.

- **Variable Costs-** There are costs like electricity charges, stationary expenses, etc. in an institution which can vary if the productions increased by the producers. These are variable costs. These costs vary directly in proportion to the change in the level of activity. If the level of operation increases, these costs increase and if the level of operation decreases the costs also decrease proportionately. For example, if a school has two shifts operating in the morning and evening using the same facilities, then the electricity, water, petrol consumption and school transport will increase, these will influence the cost too. These are variable costs.

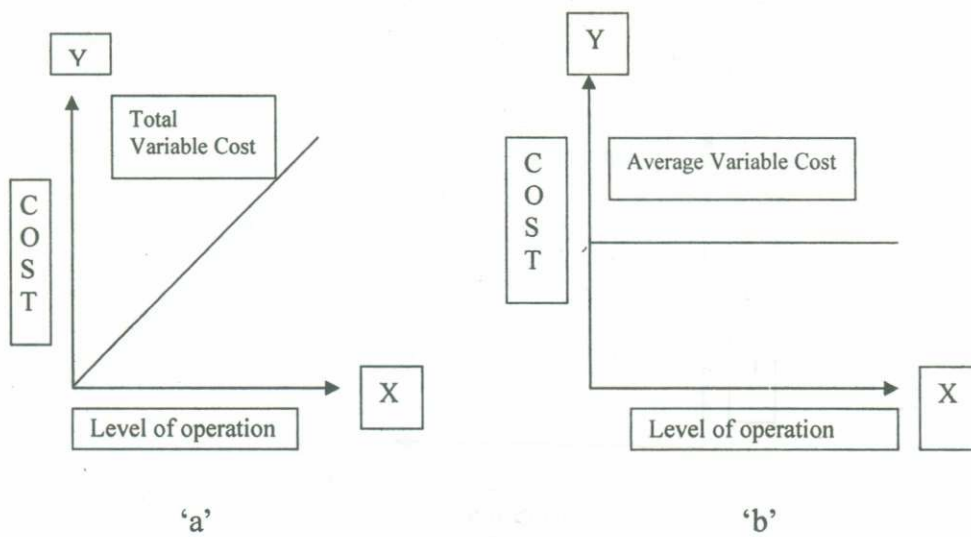


Figure 7.2 : Variable cost

- Semi-Variable Costs-** These are also known as **mixed costs**. These costs increase with the increase in operation but not as proportionately and decrease with the decrease in operation but less than proportionately. Practically, majority of costs belong to this category. For example, telephone expenses consist of a fixed rental charges irrespective of the calls made and variable charge consists of number of calls made. This phenomenon can be shown with the help of the following figure 7.3

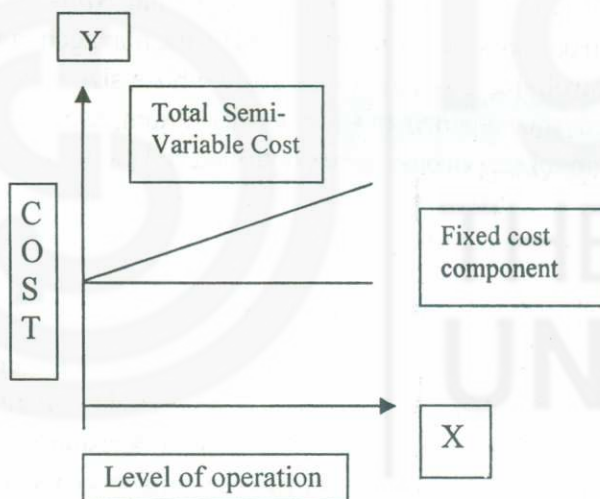


Figure 7.3 : Semi-Variable Cost

- Step Costs-** These are the costs which remain fixed till a certain point of operation. As soon as the level of operation exceeds this point, it leads to increase in cost. Then the costs remain fixed for certain level of operation and if we keep on increasing the level of operation, again the costs will increase. The graph looks like steps as shown below:

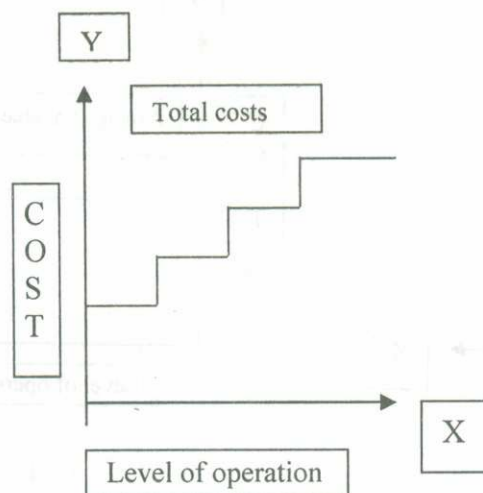


Figure 7.4 : Step Costs

Example: If as per norms there has to be one teacher for 30 students, in case we take in another student, we have to hire another teacher and if we keep on adding students, up till 60 students the costs will remain the same and after that it will increase.

7.5.2 On the Basis of Controllability

Cost can be of two types: **Controllable Costs** and **Non-controllable Costs**. Costs which can be controlled or manipulated by the management are controllable costs. Non-controllable costs are those costs whose size cannot be influenced significantly by the management or any authority. Example for Controllable costs is the number of trips of school bus can be controlled and this may reduce total number of buses involved. Examples for non-controllable costs could be the rent of the building, salaries of the permanent employees, etc.

7.5.3 On the Basis of Relevance

Costs can be classified into **relevant** and **irrelevant costs** with reference to decision-making. Cost which is influenced by a decision is a relevant cost and hence important for decision-making. Cost which is not influenced by decision-making is irrelevant. Generally in schools teachers for all compulsory subjects have been appointed on regular/full-time basis while music, arts and crafts and others hobby courses teachers as part time or visiting teachers. Here the terminology relevant and irrelevant is in the context of decision making by management.

7.5.4 On the Basis of Normality

The costs can be **normal costs** or **abnormal costs**. All costs which can be planned or budgeted are normal costs. All the unanticipated costs, which cannot be foreseen or budgeted are termed as abnormal costs. Examples: Normal- House keeping facility charges regularly. Abnormal: Damage to the institutional building by some calamities and the cost for repair is abnormal. Because it is unforeseen.

7.5.5 Other Costs Concept for Decision-Making:

- **Opportunity Cost**- Opportunity Cost represents the benefits foregone by not choosing the second best alternative in favour of the best one. The benefit that would have accrued if the second option was followed would be the opportunity cost for the alternative selected. For example, foregone rent for using own

premises would be the opportunity cost for using it for institutional purpose. These costs are not shown in financial statements but can be shown in cost-sheets as they are hypothetical costs. For example if children from economically poor families to be made to attend primary schools regularly, the management has to create incentives comparable to the income these children have to forgo. As one of the main reason for low enrollment is opportunity cost of child labour. Here parental income is too less to afford child's education and other basic needs.

- **Out of Pocket Cost-** Costs incurred or to be incurred in terms of outflow of cash due to a particular decision is out of pocket cost. In situation where the funds or resources are limited, such costs become very pertinent in the decision-making process. Example: Sometimes the schools impose extra fees under construction of school building, organizing schools functions etc.
- **Sunk Cost-** Investment of cash resources in the past decision-making are sunk costs. These cannot be changed in the future. Since, sunk costs are the results of past commitments, they should be ignored for the purpose of decision-making. The policy of management should be "don't cry over split milk". Example: The honorarium to be paid to the members fixed for attending meeting.
- **Replacement Cost-** Cost of replacing an existing machinery or equipment with an identical one is replacement cost. It includes the cost price plus the transportation cost or any other installation cost. For example, the school goes for replacement of old computers with the new ones. The cost incur in this activity is known as replacement cost.
- **Differential Cost / Incremental Cost-** This is the most important cost in decision-making process. Differential cost is the additional cost which will be incurred if the Principal or management chooses one alternative in place of another. They are in that way extra or incremental costs caused by a particular decision. For example, in the introduction of e-administration instead of manual administration the amount to be spent is this cost.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

1) What is Costing?

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2) What is fixed costs? Mention two examples of fixed costs.

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7.6 SOME BASIC CONCEPTS

Costing is defined as the '**the Process of collecting, arranging, processing and presenting costs**'. Let us now discuss some basic concepts of costing:

Cost Unit: It is a unit of quantity of product, service or time (or a combination of these) in relation to which costs may be ascertained or expressed (Institute of Cost and Management Accountants, London). For example, the cost unit in respect of educational institutions can be cost 'per student'.

Cost Centre: It is location, person or item of equipment (or a group of these) for which costs may be ascertained and used for the purpose of control (CIMA, London). A department, teaching or other personnel or equipment such as computers, projectors, etc are some of the examples of different Cost Centres.

Cost Driver: Any activity which generates cost is a Cost Driver (CIMA). For example, if a college want to initiate a new department, extra money or finance is required. Thus initiation of any project or working hours, power consumed, kilometers covered by school bus, etc are comes under cost drivers.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

3) What is variable cost? Write an example.

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4) Give an example of cost centre for an educational organisation?

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7.7 SYSTEM OF COSTING

As discussed earlier, Costing is the technique and process of ascertaining cost. The cost data should be arranged and processed in a coordinated manner according to one of the following systems :

Historical Costing

Historical costing also known as the Traditional Method, is the determination of cost by actuals i.e. actual cost incurred. It is the process of accumulation of cost in a systematic manner after the cost has been incurred. It is based on **recorded data** (vouchers) and all costs are **recorded on historical basis**. Since, past is a guide to

future, Historical cost of a product can help us to project future cost. However, it does have some limitations. It is only a post-mortem of costs incurred. Also other problem with this method is that the time gap between the period when the costs are incurred and when the data is computed, may be long so it can lead to misleading interpretations with respect to cost price of products or services. Also it does not offer a Measure of Efficiency since it does not take into account the changes in price level, change in technology, etc. Because of these limitations, Standard Costing came into existence.

Standard Costing

It is a system in which the cost of a product is ascertained in advance on the basis of certain **predetermined standards**. It deals with the costs which are yet to be incurred. They are rather **should-be** costs. Standard Costs are determined after a detailed and systematic study of costs. Once the Standard Costs are determined, the actual cost of actual output is compared with the standard cost of that output. The difference between the two accounts for a '**favorable**' or '**adverse**' variance. Hence, it is an important controlling device in the hands of management.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answer with those given at the end of this unit.

5) What are the different types of systems of costing?

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7.8 TECHNIQUES OF COSTING

Costing techniques refer to the ways in which cost data is processed and related to cost centers and cost units which in turn lead to ascertainment of cost of products and services. The following are main techniques of costing.

Absorption Costing- It is also known as the orthodox or conventional method of costing since it is the oldest method of costing. It includes charging of all costs, both variable and fixed to operations, products and processes.

Marginal Costing- Under Marginal Costing, only the variable costs are treated as Product Cost but fixed costs are treated as Period Costs. Therefore, only variable costs are charged to products, operations and processes whereas, fixed overheads are charged to the accounting period in which such costs are incurred.

Uniform Costing- It is a technique in which standardized principles and methods of cost accounting are employed by a number of undertakings related in some way for example institution falling under same industry or institutions under same regulatory authority. This technique facilitates comparisons between firms w.r.t. costs, controls, pricing policies, comparative performance, etc.

Activity Based Accounting (ABC)- A form of cost accounting that focuses on the costs of performing specific functions (processes, activities, tasks, etc.) rather than on the costs of organizational units. ABC generates more accurate cost and performance information related to specific products and services than is available to managers through traditional costing approaches. Activity Based Costing

is based on a simple principle: **activities consume resources and customers consume activities**. Associating the labor and overhead expenses of the business with the activities that consume those resources provides valuable facts. ABC defines categories of activity in overhead departments, which on the one hand are recognizable to overhead department managers but, on the other hand, are driven by factors (cost drivers) which are characteristic of products and other cost objects. This allows a much higher proportion of total company cost to be allocated to products according to causation. Ultimately, ABC provides accounting data points that can be used to improve decision-making and identify cost improvement opportunities. The basic building blocks for ABC are activity accounting spreadsheets for each element of a business. The workload of each activity is measured resulting in a cost per output.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answer with those given at the end of this unit.

6) Enumerate any two main techniques of costing.

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7.9 METHODS OF COSTING

As you have read in the earlier section that costing is the '**the process of collecting, arranging, processing and presenting costs.**' The principles in every type of costing are the same but the method of analyzing and presenting the costs differ with the nature of business. The choice of a method of costing depends upon the **nature of product, industry or service**. Though there are many methods like **Job Costing, Contract Costing, Batch Costing** and many more, but we shall concentrate on the method suitable for educational institutions which is **Operating Costing or Service Costing**. This method is suitable for enterprises indulging in rendering of services like educational services, medical services, catering and hotel services, transport companies etc. Operating Costing is used for ascertaining cost of all services within an undertaking. In this method in order to calculate the cost per unit of service rendered, the total cost incurred in a period on a service is divided by the total number of cost units of the service. For educational institutions the cost unit can be cost per student. Various costs can be categorized in various ways as follows:

Standing Costs- These costs are of fixed nature over a period of time. They do not change with the change in the number of students or the number of working days. For examples include rent of building, insurance premium, salary of staff and other permanent employees.

Maintenance Charges- These are of semi-variable nature and include costs such as repair and maintenance of computers, other equipment, cars, buses, electrical fittings, maintenance and upkeep of lawns, play grounds, laboratory perishable items, etc.

Operating or Running Costs- These costs relate to actual running of the institution and include costs on stationary, refreshment, guest lectures, conduction of activities, electricity, etc. These are directly proportional to the number of days or working hours worked in the institution.

COST SHEET*For ABC Institute of Education*

PARTICULARS	AMOUNT (per annum)
<u>Annual Total Cost:</u>	
<i>Standing Costs-</i>	
1. Salaries of Staff	
2. Rent	
3. Insurance	
4. Repairs and Maintenance	
5. Upkeep of rooms and lawns	
<i>Operating / Running / Variable Costs-</i>	
1. Power and electricity	
2. Refreshments	
3. Hospitality charges	
4. Honorarium for special Lectures or Activities	
5. Cost of running School buses, vans, cars etc.	
6. Cost of up-gradation of equipment (eg. Computers)	
7. Electrical Fittings	
8. Depreciation of fixed assets	
9. Any other cost	
<i>TOTAL COST</i>	

$$\text{Therefore, Cost per Student} = \frac{\text{Total Cost} + \text{Surplus}}{\text{Total number of Students}}$$

Example 1:

From the following particulars, calculate the cost relating to a charitable school. Also calculate cost per student assuming that the strength of the school is 1200 and the school includes a surplus of 10% on cost as a means of meeting any contingency.

- (1) Salaries of Staff Rs. 8,00,000 p.a.
- (2) Wages of Class Attendant Rs. 4500 p.m.
(There is one attendant for every 2 classrooms)
- (3) Lighting and Power:
 - a) For each classroom the lighting expenses are Rs. 200 p.m.
 - b) For offices and other rooms the lighting expenses are Rs. 300 p.m.
 - c) For Computer Lab the expenses are Rs. 500 p.m.

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|---|--------------------|
| (4) Repairs to Building | Rs. 1,00,000 p.a. |
| (5) Curtains, Sheets and other supplies | Rs. 48,000 p.a. |
| (6) Sundries | Rs. 66,000 p.a. |
| (7) Maintenance and upkeep of lawns
(It includes the wages of gardener also) | Rs. 10,000 p.a. |
| (8) Depreciation @ 5% is to be charged on building costing | Rs. 40,00,000 p.a. |

There are 50 classrooms in the school and there are 10 other rooms including offices, Principal's office and other laboratories. There is however only one computer laboratory.

COST SHEET OF A CHARITABLE SCHOOL

PARTICULARS	AMOUNT (per annum) in Rs.
Total Annual Cost:	
<u>Fixed Costs:</u>	
Salaries	8,00,000
Wages of attendant (50 rooms / 2 = 25 attendants) (25 attendants × Rs. 4,500 × 12 months)	1,35,000
Repairs to Building	
Depreciation on Building @ 5%	1,00,000
<u>Variable Costs:</u>	2,00,000
Lighting Classrooms (50 × 200 × 12) =	1,20,000
Offices (10 × 300 × 12) =	36,000
Computer Lab. (500 × 12) =	6,000
Curtains, Sheets etc	1,62,000
Sundries	48,000
Maintenance and upkeep of lawns	66,000
	10,000
TOTAL COST	15,21,000

Therefore, the cost per student will be

$$\frac{15,21,000 + 1,52,100}{1200} = \text{Rs. 1394.25 per student}$$

Here an attempt has been made to acquaint you with the methods of costing and a common format cost sheet of an educational organisation. Cost sheet of a charitable school has been presented as an exemplar.

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

7) Write the formula for calculating the cost per student.

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8) What is standing cost? Give an example of standing cost from a government run school.

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7.10 BUDGETING

We all are familiar with the term Budgeting. Budgets are important tools of financial planning. Every organisation needs to make basic decisions about how it will allocate its resources. An explicit planning is required for setting goals, determining resource allocation patterns, and deciding what program services will be provided. In wake of these requirements, a budget is required to be prepared. A Budget can be defined as a ***“comprehensive and coordinated plan, expressed in financial terms, for the operations and resources of an enterprise for some specified period in future”***. Budgets are an important tool of financial planning of any organisation. Budgeting, as a tool of planning, is closely related to the broader system of planning in an organisation

CIMA, London has defined Budget in a very comprehensive manner as follows-

“A financial and/or quantitative statement prepared and approved prior to a defined period of time, of the policy to be pursued during the period for the purpose of attaining a given objective. It may include income, expenditure and the employment of capital.”

Main features of Budgets

The main features of budgets have been given below:

- ***It's a plan-*** Budget is a plan- comprehensive and coordinated, for a specific period of time in future. It is prepared much in advance for the stipulated period.

- **Expressed in financial terms-** Budgets are prepared in terms of monetary value such as rupee, dollar or any other currency. Expressing everything in terms of money provides a common denominator to compare diverse activities and operations.
- **Specified future period of time-** The period is usually one accounting period but budget can also be drawn on a monthly or quarterly basis.
- May be related to **incomes, expenses, capital receipts and capital expenditures.**
- Basically **relate to planned events.** They refer to policies and programmes to be pursued by any organization.
- **Lay down the objectives** to be pursued by any organization and are an important tool for planning, coordinating, directing, motivating and controlling in the hands of management.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answer with those given at the end of this unit.

9) What are the key features of a budget?

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7.11 WHY DO WE NEED BUDGETS?

In educational institution, Budgets serve as a guide to the conduct of operations and a basis for evaluating actual results. Preparation of Budgets serves the following purpose:

Statement of Expectations- A budget is a device to express goals or objectives to be achieved in a stipulated period of time. They formulate targets of expected performance. They explicitly communicate the expectations of the management regarding goals or objectives to be pursued in the forthcoming period.

Communication- Budgets are generally prepared by the management of any institution. By way of Budgets they can effectively communicate to their employees and other stakeholders, the direction in which the efforts of the institution have to be channelized.

Coordination- A major function of Budgeting is coordination. Coordination refers to the operation of all departments in an institution in connivance with each other so that there are no bottlenecks in the smooth functioning of the institution. Budgets should be drafted in such a manner that the operations of different departments are related to each other for the achievement of overall goal of institution.

Controlling- Since a budget establishes expectations, defines the goals and the means of achieving them, it serves as a very effective controlling device. We can judge the operations of different departments and individuals and compare them to the standards. However, *budget should not be regarded as a rigid requirement of performance. It should be regarded as a plan, not as an ultimate commitment of performance.*

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answer with those given at the end of this unit.

10) Explain the need of budgets by any educational institutions?

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7.12 TYPES OF BUDGETS

We shall now look into the different types of budgets. Please see the figure 7.5 Types of Budgets given in the following:

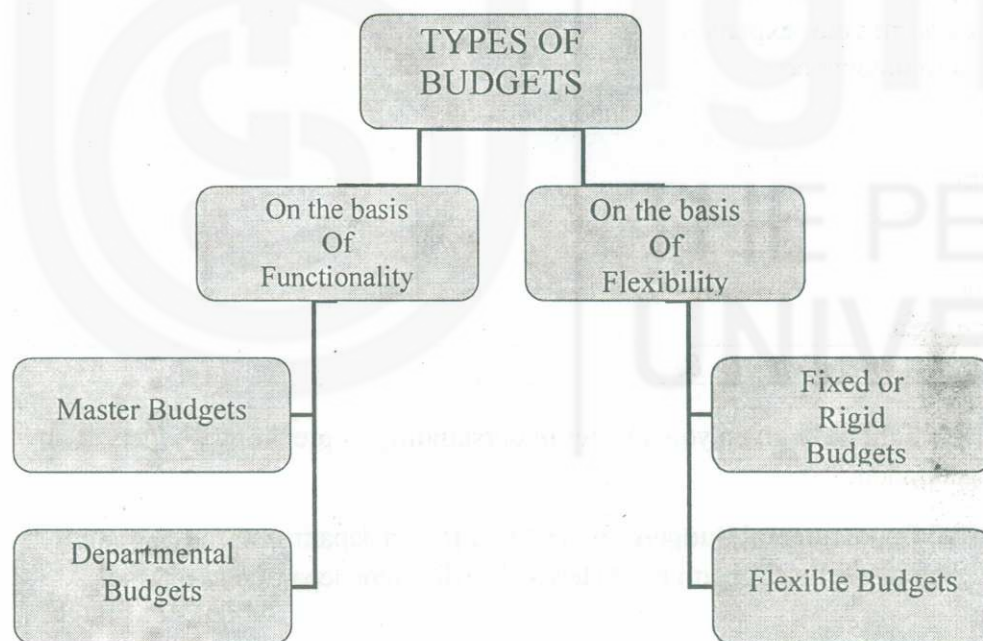


Figure 7.5: Types of Budgets

Let's now discuss each of these briefly:

7.12.1 Master Budgets- An institution's Master Budget projects the overall financial and operating plan for a forthcoming fiscal period. It is generally prepared annually. It is very comprehensive in nature as it includes all possible sources of incomes and expenditures. It is the end-product of all the budgeting process and is generally prepared after all different Departmental Budgets have been prepared. An example of a format of a Master Budget is given below:

PARTICULARS	BUDGETED FIGURES In Rs (prev. year)	BUDGETED FIGURES In Rs (current. year)	Difference (in percentage)
<u>Estimated Fund Balance (Opening)</u>			
<i>(A) Receipts and Revenues:</i>			
1. Fees			
2. Donations			
3. State or any other Grant			
4. Rent received			
5. Interest on deposits			
6. Membership fee received			
7. Any other receipts			
<i>(B) Disbursements and Expenses:</i>			
1. Regular employee salary (teaching)			
2. Regular employee salary (administrative staff)			
3. Guest teacher or ad-hoc staff			
4. Overtime salary			
5. Insurance			
6. Any special event expenses (fetes, excursions, etc.)			
7. Rent paid			
8. Local travel			
9. Different Departmental expenses			
10. Repairs and maintenance			
11. Stationary			
12. Postage			
13. Other supplies			
14. Telephone expenses			
15. Electricity			
16. Equipment			
17. Any other expense			
<i>Budgeted Net Surplus or Deficit (A - B)</i>			

This might have given you a better understanding of preparing budgets of any organisation.

7.12.2 Departmental Budgets: Budgets of different departments must be prepared by their respective Departmental Heads. The different departments may be-

- i. Primary Section
- ii. Secondary Section
- iii. Higher Secondary Section
- iv. Senior Secondary Section

Or the institution may prepare subject-wise department budgets like:

- a. Languages Department
- b. Physical Sciences Department
- c. Biological Sciences Department

d. Social Science Department

Or in the institutes of Higher Education, faculty-wise budgets may be prepared:

- a. Arts Stream
- b. Commerce Stream
- c. Sciences- Physical and Biological
- d. Physical Education
- e. Theatre and Dramatics etc

The format of a departmental budget is given below:

PARTICULARS	BUDGETED FIGURES In Rs (prev. year)	BUDGETED FIGURES In Rs (current year)	Difference (in percentage)
Receipts: 1. Grant / Donation 2. Fund Allocation Expenditures: 1. Laboratory Expenses 2. Library 3. Periodicals, Journals, etc 4. Teaching Material bought 5. Excursions or field trips etc 6. Seminars or work-shops conducted 7. Faculty Enrichment Programme 8. Any additional /new activity conducted during the period. 9. Any other expense			

7.12.3 Fixed Budgets: A Fixed Budget is prepared for a fixed level of anticipated operation. According to CIMA “a budget which is designed to remain unchanged irrespective of the level of activity actually attained is a fixed budget”. It is based on the assumption that an institution can accurately and precisely forecast the level of its operation in a specified period of time. The format of budgets discussed under Master and Departmental Budgets can be taken up as examples of fixed budgets.

7.12.4 Flexible Budgets: These are also known as *Variable* or *Sliding* or *Dynamic Budgets*. It is geared towards reflecting different levels of operation and activities. The merit of flexible budgets is that instead of one estimate it contains several estimates or plan in different conditions or situations. It works on the assumption that since future is unpredictable, therefore operations of an institution cannot be predicted with absolute certainty. Therefore, flexible budgets provide a more realistic basis of budgeting. So we can say that as a tool of planning and control, they are superior to fixed budgets as they present costs at different levels of activities. The format is discussed as under:

PARTICULARS	PESSIMISTIC	MOST LIKELY	OPTIMISTIC
A. Revenues			
B. Fixed Costs			
C. Variable Costs			

Check Yours Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

11) What is budget?

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12) What is fixed budget?

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7.13 BUDGETARY CONTROL

Budgetary Control is a *system of management and accounting control by which all operations – revenues and expenditures are forecasted as far ahead as possible and the actual results when known are compared with the budget estimates*. This implies after the stipulated period, for which budgets were drawn, is over, the actual results are compared to the estimates and the variance is calculated. Also the reasons for deviations are looked into. Therefore, the use of budget and the budgetary process for planning, coordination and control is known as budgetary control.

Advantages of Budgetary Control

A system of budgetary control is very important for any institution to work in a systematic and coordinated manner. It helps the management in its different functions at various stages like Planning, Organizing, Coordinating, Directing, Motivating and Controlling. The main points are summarized as under-

- Budgets help in fostering a systematic and disciplined approach to problem-solving based on comprehensive advance planning.
- It forces the management to identify the objectives, prioritize them and work on them in an orderly manner.

- Budgets invariably bring efficiency in any organisation and it helps as a great tool of financial discipline.
- It forces the institution to foresee problems well in advance and hence ways and means of dealing with them.
- It helps in better coordination between different levels of management and different departments.
- It boosts the spirit of team cooperativeness.
- It helps in making optimum use of resources- their allocation and utilization.
- It is also a great motivational tool.
- It provides ground to management to reintrospect their future plans, policies and revise and reformulate them.
- They also help in bringing about uniformity in the entire system of functioning of the institution.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

13) Explain the term budgetary control?

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14) Write any two advantages of budgetary control?

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7.14 LET US SUM UP

In this unit we dealt with cost and budgeting . As we know that every institution or organization tries to raise the financial resources. To maximize this it is every institution to calculate the institutional cost and budgeting. Actually cost refers to the amount of resources expense for producing a product or for rendering a service, the resources may be material equipment, transport, salaries, rent, power, etc. On the other hand budgeting is an important tools of financial planning. It is an important task of any organization or institutions to prepare a financial budget at preliminary level for a stipulated period. We focused on how an institution will develop with the help of costing and budgeting methods. In the advancement of the society , it is very necessary to upholding the institution, the principal would keep in mind core concept of costing and budgeting teaching and methods, and modification or replacement could be most welcome.

7.15 UNIT END ACTIVITIES

Select any educational institution. Study the financial budget heads and analyse them. Write a report highlighting the advantages and limitations of their financial estimates of an academic year.

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7.17 ANSWERS TO CHECK YOUR PROGRESS

- 1) According to CIMA, costing is the technique and process of asserting cost. It is the process of estimating cost for items in a programme.
- 2) Cost which do not change with the increase or decrease in the level of operation are fixed cost. The examples includes rent of premises, salary of permanent employees, etc.
- 3) Ref. subsection 7.5.1
- 4) Ref. section 7.6
- 5)
 - a) Historical costing
 - b) Standard costing
- 6)
 - a) Absorption costing
 - b) Marginal costing
 - c) Uniform costing
- 7)
$$\text{Cost per Student} = \frac{\text{Total Cost} + \text{Surplus}}{\text{Total number of students}}$$
- 8) Ref. section 7.9
- 9) The main features of budgets have been given below:

- **It's a plan-** Budget is a plan- comprehensive and coordinated, for a specific period of time in future. It is prepared much in advance for the stipulated period.
- **Expressed in financial terms-** Budgets are prepared in terms of monetary value such as rupee, dollar or any other currency. Expressing everything in terms of money provides a common denominator to compare diverse activities and operations.
- **Specified future period of time-** The period is usually one accounting period but budget can also be drawn on a monthly or quarterly basis.
- May be related to **incomes, expenses, capital receipts and capital expenditures.**
- Basically **relate to planned events.** They refer to policies and programmes to be pursued by any organization.
- **Lay down the objectives** to be pursued by any organization and are an important tool for planning, coordinating, directing, motivating and controlling in the hands of management.

10) In educational institution, Budgets serve as a guide to the conduct of operations and a basis for evaluating actual results. Preparation of Budgets serves the following purpose:

Statement of Expectations- A budget is a device to express goals or objectives to be achieved in a stipulated period of time. They formulate targets of expected performance. They explicitly communicate the expectations of the management regarding goals or objectives to be pursued in the forthcoming period.

Communication- Budgets are generally prepared by the management of any institution. By way of Budgets they can effectively communicate to their employees and other stakeholders, the direction in which the efforts of the institution have to be channelized.

Coordination- A major function of Budgeting is coordination. Coordination refers to the operation of all departments in an institution in connivance with each other so that there are no bottlenecks in the smooth functioning of the institution. Budgets should be drafted in such a manner that the operations of different departments are related to each other for the achievement of overall goal of institution.

Controlling- Since a budget establishes expectations, defines the goals and the means of achieving them, it serves as a very effective controlling device. We can judge the operations of different departments and individuals and compare them to the standards. However, *budget should not be regarded as a rigid requirement of performance. It should be regarded as a plan, not as an ultimate commitment of performance.*

11) Budgets are important tools of financial planning. A budget can be defined as a comprehensive and coordinated plan, expressed in financial terms, for the operations and resources of an organisation for the operations and resources of an enterprise for some specified period in future. According to ICMA, "A financial and/or quantitative statement prepared and approved prior to a defined period of time, of the policy to be pursued during the period for the purpose of attaining a given objective. It may include income, expenditure and the employment of capital"

- 12) A fixed budget is prepared for a fixed level of anticipated operation. According to CIMA "a budget which is designed to remain unchanged irrespective of the level of activity actually attained is a fixed budget.
13. Budgetary control is a system of management and accounting control by which all operations – revenues and expenditures are forecasted as far ahead as possible and the actual results when known are compared with the budget estimates. This implies after the stipulated period, for which budgets were drawn is over, the actual results are compared to the estimates and the variance is calculated. Also the reasons for deviation are looked into. Therefore, the use of budget and the budgetary process for planning and control is known as budgetary control.
14. (i) Budgets help in fostering a systematic and disciplined approach to problem-solving based on comprehensive advance planning.
(ii) It forces the management to identify the objectives, prioritize them and work on them in an orderly manner.
(iii) Budgets invariably bring efficiency in any organisation and it helps as a great tool of financial discipline.
(iv) It forces the institution to foresee problems well in advance and hence ways and means of dealing with them.
(v) It helps in better coordination between different levels of management and different departments.
(vi) It boosts the spirit of team cooperativeness.
(vii) It helps in making optimum use of resources- their allocation and utilization.
(viii) It is also a great motivational tool.
(ix) It provides ground to management to reintrospect their future plans, policies and revise and reformulate them.
(x) They also help in bringing about uniformity in the entire system of functioning of the institution.

UNIT 8 ACCOUNTING AND AUDITING

Structure

- 8.1 Introduction
- 8.2 Objectives
- 8.3 Accounting- The Concept
 - 8.3.1 Basic Accounting Concept
 - 8.3.2 The Money Measurement Concept
 - 8.3.3 The Cost Principle
 - 8.3.4 The Matching Principle
 - 8.3.5 The Going – Concern Concept
 - 8.3.6 The Realization Concept
 - 8.3.7 The Accrual Concept
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8.1 INTRODUCTION

Any organization involved in any kind of economic activity has to maintain a systematic record of all the day-to-day transactions so as to keep a track on the financial health of the organization. Accounting is that branch of knowledge which provides us ways and means of recording all the transactions pertaining to financial character in an organization in a systematic and orderly manner. And the process of Auditing ensures

that accounts are maintained according to accepted norms. In the following pages we will study the basic postulates and practices of accounting and auditing with special reference to the educational institutions.

8.2 OBJECTIVES

After studying this unit, the student will be able to:

- explain the meaning and need of accounting;
- define the basic concepts of accounting and discuss their importance;
- analyze the importance of Accounting Equation and the impact of it on various transactions;
- discuss the dual aspect of debit and credit for every transaction and the importance of doing so;
- understand the process of Accounting Cycle;
- prepare Journal, Ledger and Trial Balance from any given transactions;
- prepare Financial Statements for any educational institution;
- discuss upon the concept and importance of auditing;
- state the objectives of auditing;
- discuss the scope and types of auditing; and
- discuss the importance of audit report.

8.3 ACCOUNTING – THE CONCEPT

A complete and comprehensive definition of Accounting has been given by the American Institute of Certified Public Accountants (AICPA) as follows:

“Accounting is the art of recording, classifying and summarizing in a significant manner and in terms of money transactions and events which are, in part at least of, financial character and interpreting the results thereof.”

Accounting is often referred to as the **“language of business”**. Accounting is the common language used to communicate financial information to individuals, organisations, Governmental agencies and so on about the various aspects of business and its financial position. Accounting information is needed by two sets of users-internal and external. *Internal users* are associated with management of the concern for which information is sought to be gathered and surveyed and *external users* consist of several explicit groups. The users of accounting information are specified as follows:

USERS OF ACCOUNTING INFORMATION

• INTERNAL USERS

- Board of Directors
- Partners
- Managers
- officers

• EXTERNAL USERS

- Investors
- Lenders
- Suppliers
- Governmental agencies
- Employees
- Customers
- Regulatory authorities
- Legislators
- Researchers

In a nut shell we can say that -

- Accounting is a science as well as an art but more importantly it is a profession.
- The process of accounting includes the steps of recording, classifying and summarizing financial transactions and events.
- The process of accounting is executed based on certain rules, principles and concepts.
- The process of accounting takes place in certain books known as the 'Books of Accounts' and the major Books of Accounts are Journal, Cash Book, Ledger etc.
- Accounting is used to communicate financial information to its various users.
- The accountants have to meet the requirement of various laws such as Companies Act, Income Tax Act and laws framed by other regulatory bodies from time to time.
- Accounting enables to forecast the future performance and financial position using past accounting information and it provides vital data on the basis of which the managers take vital decisions.

A Story for Relating to Accounting Basics

We will present the basics of accounting through a story of a person new to field of accounting. The person is Vipin Chandra—a savvy man who is a visionary and has a number of ideas relating to the ways in which an educational institution can be made and run successfully. He along with his associates form a society and plan to run an educational institution. They all are hard workers, but admit that they are not comfortable with matters of accounting. They want to understand the financial statements prepared in an educational institution and wants their school to be on the top. Their attorney recommends Ms. Nair, an accountant who can help them understand the nitty-gritty of accounting. In his first meeting with Ms. Nair, Vipin Chandra asks her for an overview of accounting procedures, basic accounting procedures, and the different financial statements to be prepared. Let us briefly discuss some of the very basic concepts on which the whole system of accounting is based.

8.3.1 Basic Accounting Concepts

Accounting is not an exact science like Physics or Mathematics where methods can be validated by natural laws. The process of accounting is executed on the basis of certain principles, rules and concepts. Therefore, a set of Generally Accepted Accounting Principles (GAAP) provide a unity of understanding and also unity of approach in the practice of accounting. The term 'generally accepted' means that these principles must have solid support of the professional accounting bodies like ICAI (Institute of Chartered Accountants of India). Now let us briefly discuss the basic accounting concepts:

The Entity Concept

Fundamental Question:

Mr, Vipin Chandra and his associates have invested money, in a school. And since the school belongs to them so are they different financially from the school ?

Ms. Nair makes them understand that this question basically relates to a fundamental concept also known as "Separate Entity Concept". It says that *the business* and its *owners* are *two separate or distinct entities*. Both of them have their separate accounting existence. The owners are treated as creditors for the investment they have made in the business. The capital of the owners is always treated as a liability of the business. Each business has its own earnings and revenues and incurs its own expenses and owns its own assets and liabilities. So the school has separate legal existence from its owners.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

- 1) Mention two internal and external users of accounting.

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- 2) What is GAAP ?

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8.3.2 The Money Measurement Concept

Fundamental Question:

Do the books of accounts take into consideration all events and happenings in an organization? For e.g a new director joining or a teacher/principal leaving?

No, even if an important event like joining or leaving of a director occur, it will not find a place in the books of accounts. Of course, the financial aspect of it like Payment of gratuity, leave encashment etc. will be recorded. Ms. Nair explains that Money Measurement Concept is an assumption that all business transactions are expressed and recorded in terms of money. This means that *money is the only media* which can be used to record financial transactions. And so only those transactions and events which can be measured in terms of money can be recorded in the books of accounts.

8.3.3 The Cost Principle

Fundamental Question:

If Mr. Chandra purchases a building for the institution valued at Rs. 15 lakhs from a builder friend at Rs. 12 lakhs, at what price will it be recorded in the books of accounts?

According to this principle, an asset is recorded in the books at the price paid for it and not at its market value. In accounting there is not place for personal opinions as far as the value of transactions is concerned. The effects of this cost concept are:

1. All assets are valued at *Cost Value* or the *Book Value* (which is the cost value minus the depreciation).
2. The items which have no cost are ignored, i.e. if the business has not paid for an asset, it does not appear in the books of accounts.

8.3.4 The Matching Principle

Fundamental Question:

If an institution purchases furniture and equipment for Rs. 15 lakhs in 2005 which is expected to function for the next 10 years, should the whole amount of Rs. 15 lakhs be charged in the books of accounts of 2005?

No, the cost of the furniture will be divided over a span of 10 years that is its life span. This principle matches the earnings for a period with the expenses incurred in order to make those revenues. This principle is applied while calculating profit or loss for an accounting period. Calculation of income or profit is a matter of matching the revenues with the respective expenses and we have to take into account all costs- direct and indirect in order to arrive at the true value of profit.

So, if we have purchased an asset, which we are likely to be used for a considerable number of years to come, if the entire cost is considered in the first year's income statement, there will be a huge burden in the income statement of the first year and no burden at all in the subsequent years (whereas the firm is earning revenues on account of usage of this asset). In other words, there will a mismatch between the revenue earned from the asset and the cost incurred for the machine. The matching principle matches the earnings for the period and the expenses incurred to earn these earnings. So the cost of the asset has to be allocated to its total span of useful years.

8.3.5 The Going-Concern Concept

Ms. Nair also explained this simple but important concept that an enterprise or an accounting entity has an endless life. It means that if an organisation is set-up, the purpose is to run it forever. It will not be dissolved or liquidated in the immediate future until and unless there is a clear evidence to the contrary. This assumption or concept is important as it provides for sound accounting of long-term or fixed assets. It also facilitates classification of assets and liabilities into short-term and long-term.

8.3.6 The Realization Concept

Ms. Nair advised Mr. Chandra to keep the Realization concept in mind while preparing the final financial statements at the end of the financial year. We know that income of any organisation is measured as the excess of revenues over expenses. However, it is not always easy to determine when the revenue should be considered as realized? Is it when the goods or services are produced or when an order is received by the customer or when the goods or services are delivered or accepted by the customer or when the cash is received from him/her. There can be huge time-gap between the performances of these activities so Realization concept states that **revenue should be recognized when it has been realized** i.e. when the transaction gives a **legal right to the receipt of money**. So we can record a revenue or an earning as revenue of that period in the books if either the cash has been received against the transaction or an outside party has promised to pay. This is simple playing safe and not taking a risk of recording a revenue which is not earned.

8.3.7 The Accrual Concept

Fundamental Question:

If an income is earned but not received, should we take into account such income?

Again this concept is in consonance with the previous concept. The accrual concept is a very important accounting system which recognizes revenues and expenses as they are earned or incurred respectively without regard to the date of receipt of payment. In the income statement of an organisation revenues and expenses are recognized as they are earned or incurred respectively and it is immaterial whether the cash has changed hands or not. The essence of this concept is mere promise on the part of customer to pay money for services rendered is considered a revenue and similarly promise on the part of organization to make payment for salaries, rent etc is considered as an expense.

8.3.8 The Conservatism or Prudence Concept

Ms. Nair also told him that a good accountant is always very conservative in his/her approach. Conservatism is a prudent reaction to uncertainty to ensure that uncertainties and risks inherent in business situations are adequately considered. The rule of thumb is to "*anticipate no gains but to provide for all losses and if in doubt, write them off*". This concept requires that assets and profits should not be overstated and revenues should never be anticipated; being recognized only when there is reasonable certainty about its realization. At the same time provision must be made for all possible liabilities, whether the amount is known with certainty or is based on estimation. A prominent example of the treatment of this concept in accounts is that inventory or stock is valued at cost price or market price whichever is less. Also if there is a debt which is not likely to be realizable, a provision for bad and doubtful debts is set aside to meet any contingency.

8.3.9 The Convention of Full Disclosure

Accountants are unanimous that there should be full, fair and adequate disclosure of all financial information. Thus this concept pertains to communication and reporting of accounting and non-accounting information to various direct and indirect users for the purpose of their analysis and decision-making. It implies that no information of substance or interest to the average investor will be omitted or concealed.

Fundamental Question:

Mr. Chandra purchased furniture worth Rs. 5 lakhs for the school. Now how this transaction should be recorded- as furniture added or as cash going out of the organisation?

8.3.10 The Dual Aspect Concept:

This is an *extremely important* concept. The understanding of the whole accounting process is based upon this concept. According to this each and every transaction has dual aspect and in the books of accounts both the aspects have to be shown properly. For an example, Mr. Chandra and his associates when starting the school invested a sum of Rs. 20 lakhs cash. Now as per the entity concept, we know that Mr. Chandra and his institution are two distinct accounting entities. Since we are trying to understand accounting for institutions, so we will be discussing the books of accounts of the school or the institution. In the books of accounts of the school the transaction would be

Cash received from Mr. Chandra and associates Rs.20,00,000 as capital.

We can see that it has got a dual aspect: (1) cash coming in and (2) institution owing Rs. 20 lakhs to its proprietors i.e. the society formed.

Similarly, if furniture worth Rs. 50,000 has been purchased, again the two aspects would be (1) Rs. 15,000 paid as cash and (2) furniture coming in. We will discuss this in detail in the following pages.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

3) What is Separate Entity concept in response to business?

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4) What is the process of Accounting ?

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5) Who are the users of accounting information?

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8.4 THE BASIC ACCOUNTING EQUATION

In a business organization the total *of assets is always equal to its liabilities*. This is the basic Accounting Equation. Each and every transaction will have an impact on the equation but in every case assets will always be equal to liabilities. Let us observe the above situation:

Mr Chandra investing Rs. 20 lakhs in the institution: this implies there is cash coming in and the business owing the amount to Mr Chandra, the proprietor.

So	Assets	=	Liabilities
Therefore,	Cash (20 Lakhs)	=	Owners' claim/Capital
	(Rs. 20 lakhs)		

Further, furniture was purchased for Rs. 5 lakhs. Since furniture is an asset, we can show it as:

Assets	=	Liabilities
Cash (20,00,000- 5,00,000)		
+Furniture (5,00,000)		
	=	Rs. 20,00,000

Now further Laboratory Equipment worth Rs. 7,00,000 was purchased. Again, we know that Laboratory Equipments are assets for the organisation, we can show the changes in the equation as under:

Assets	=	Liabilities
Cash (15,00,000-7,00,000)		
+Furniture (5,00,000)		
+ Lab. Equipment (7,00,000)	=	Rs. 20,00,000

NOTE: There has been no change in the value of Liabilities as there has been no transaction which affects the state of Liabilities.

Now say, the institution's library needs to be set up and the cost of setting up the library comes out to be Rs. 8,00,000. Mr. Chandra decides to take a loan for the purpose from a bank. The effect on the equation would be:

Assets	Liabilities
Cash 16,00,000 (8,00,000+ 8,00,000)	Capital (20,00,000)
+ Furniture (5,00,000)	+ Bank Loan (8,00,000)
+ Lab. Equipment (7,00,000)	Therefore, TOTAL LIABILITIES = 28,00,000
Therefore, TOTAL ASSETS = 28,00,000	

In order to show both the aspects of any transaction, we follow the **double entry system**. Double entry is a simple yet powerful concept: each and every one of a company's transactions will result in an amount recorded into **at least two** of the accounts in the accounting system where one account is debited and the other is credited.

8.4.1 Debits and Credits

Ms Nair introduced them to very important concepts of debit and credit used in the double entry accounting. Rather than using a single column for each account and entering some numbers as positive and others as negative, we use *two columns for each account*. Whether the entry increases or decreases the account is determined by choice of the column in which it is entered. Entries in the left column are referred to as **debits**, and entries in the right column are referred to as **credits**. Two accounts always are affected by each transaction, and one of those entries must be a debit and the other must be a credit of equal amount. In accounting, the verbs "debit" and "credit" have the following meanings:

<u>DEBIT</u>	<u>CREDIT</u>
Means "enter in the left column of"	Means "enter in the right column of"

8.4.2 Types of Accounts and the Debit-Credit Rules

The rules of Debit and Credit can be explained further according to different of accounts. All accounts can be classified as either a **Real Account**, or a **Nominal**

Account or a **Personal Account**. And all these different types of accounts have their own rules of debit and credit as explained under:

S.No.	TYPE OF ACCOUNT	DESCRIPTION	EXAMPLES	RULE OF DEBIT AND CREDIT
1.	Personal Account	Account of persons-natural or artificial. A person can either give or receive something.	Proprietor's A/c, Seller's A/c, a Creditor's A/c	Debit the receiver and credit the giver.
2.	Real or Property Account	Account of things which are real but lifeless. A thing may either come into the business through buying or go out of it through selling.	Cash A/c, Building A/c, Equipment A/c, Machinery A/c etc.	Debit what comes in and credit what goes out.
3.	Nominal or Fictitious Account	These are accounts of expenses, losses or gains and incomes.	Wages A/c, Interest A/c, Salaries A/c, Fees A/c, Misc. Expenses A/c, Donations A/c etc.	Debit all expenses and losses and Credit all incomes and gains.

Another very important step in understanding Accountancy is to understand a few very significant and basic concepts which are explained below:

8.5 FEW BASIC CONCEPTS TO BE UNDERSTOOD

8.5.1 Income Measurement

Income is a synonym of Net Profit but in case of educational institutions, since most of them are non-profit organisations, we do not use the term profit. Also in the further pages we would be dealing with the accounts as per the norms of Not-for-Profit Organisations. **Income is the increase in the net worth** of an organisation. Net worth is calculated by subtracting the outside liabilities from the assets of the organisation.

So, Net Worth = Assets – Outside Liabilities

And if we subtract the net worth of a concern in the beginning of the accounting period and at the end, the difference would be the income for the period. For calculating the income of the period we prepare the Income and Expenditure A/c.

8.5.2 Capital and Revenue Items

It is very important to distinguish between the capital and revenue items. The term 'Revenue Items' is different from the concept of revenue. Revenue indicates earnings for an organization like in case of an educational institution, it can be fees, donations, and other funds received. On the other hand revenue items indicate revenue expenses and revenue receipts. Let us discuss each of them in detail:

- **Capital Items:** They include capital expenditures and capital receipts. Capital expenditure is an expenditure which is incurred (i) to buy a fixed asset, (ii) increase the useful life of fixed asset, (iii) increase the productivity of fixed assets, or (iv) making an asset usable or reusable. Capital Receipts are those receipts which are collected from the sale of old fixed assets, sale of investments, issue of shares, debentures or raising loans etc. These are of non-recurring nature. They are basically shown in the Balance Sheet.
- **Revenue Items:** Revenue expenses are those expenses which are incurred in the usual course of business on a regular basis. These are of recurring nature. For e.g. payment of salaries, wages, rent, taxes, insurance etc. **Revenue incomes** are those which are collected in usual course of business on regular basis. e.g fees collected, interest earned, commission received, donations received etc. These items are taken into consideration while calculating the income for an accounting period.

8.5.3 Deferred Revenue Expenditure

Sometimes, the amount involved in the revenue expenditure is very heavy. If such expenditure is charged fully in the income statement of a year, it will result in heavy reduction of profit of that year. Therefore, only a part of such expenditure is shown in the income statement every year and the balance is shown in the balance sheet since their benefit is likely to accrue in many years to come. The examples may be expenditure on advertisement etc.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

6) Explain the term income measurement.

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7) Differentiate between capital and revenue items.

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8.6 THE ACCOUNTING CYCLE

Now let us have a look at the basic accounting cycle. The sequence of activities beginning with the occurrence of a transaction is known as the **accounting cycle**. This process is shown in the following Figure 8.1.

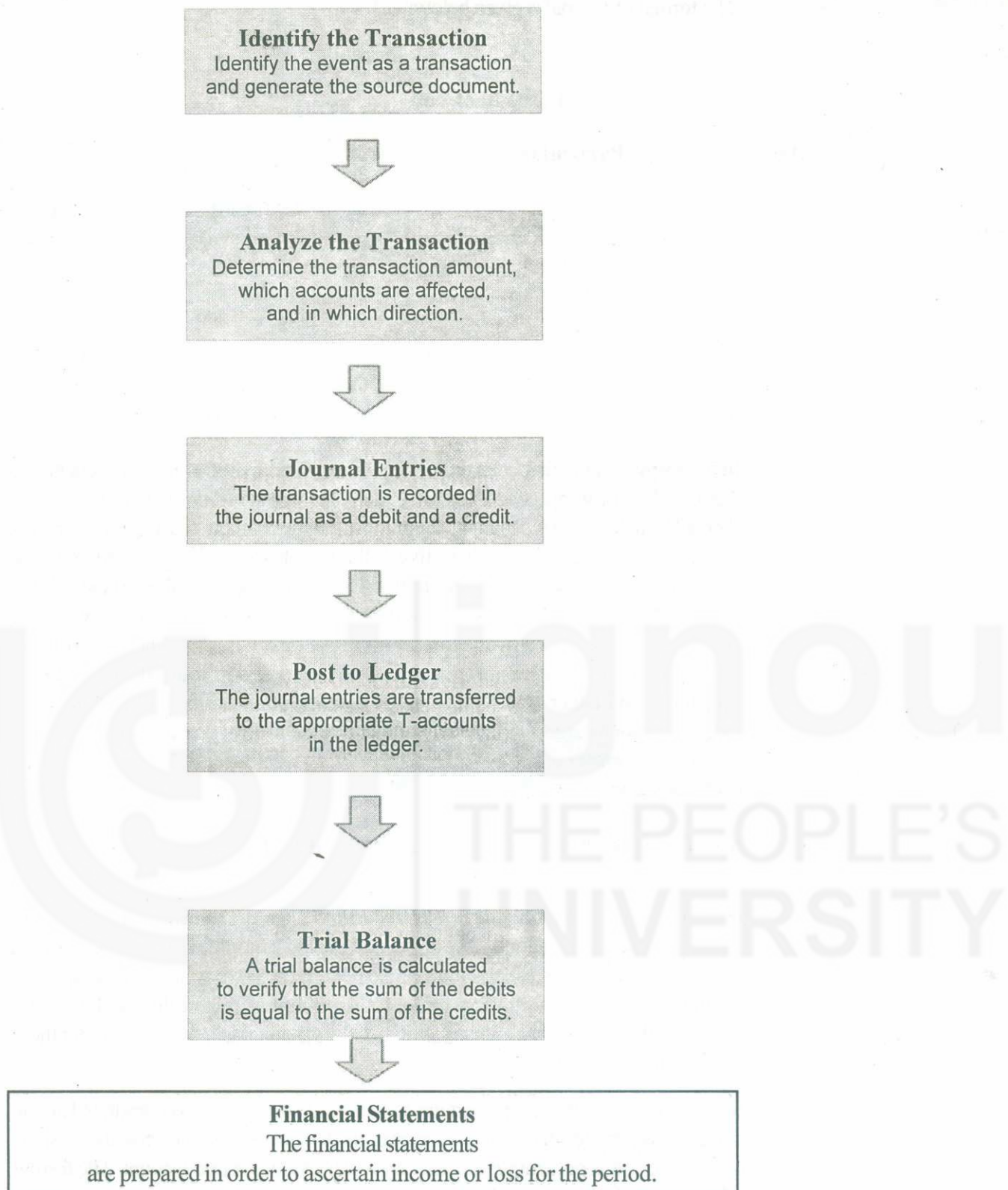


Figure 8.1: Steps in the Accounting Cycle

Study the Accounting Cycle carefully. Let us now discuss each of these steps in some detail. There are two records very significant in the accounting process. These are **Journal** and **Ledger**. After preparing these records, we prepare the **Trial Balance** and at the end of the financial year, we prepare the **Final Accounts**. Each of these steps are discussed below in detail.

8.6.1 Journal – book of original entry

Having discussed the concepts of Debit and Credit and the Accounting Cycle, let us

first of all discuss the *very first* and *important book of original entry* i.e. Journal.
The format of Journal is given below:

Journal

In the books of _____

J.V. No.	Date	Particulars	L.F.	Amount	
				Debit	Credit

In the format, in the first column we note down the number of Journal Voucher. In this voucher the transaction is shown exactly the way it is recorded in Journal. The Journal Voucher (JV) is signed by the authorized signatories of each department and is supported by actual vouchers like bills, receipts etc. These JV become the authenticated document for recording all transaction in the Journal. The next column is the date on which the JV is prepared. In the 'Particulars' column we write the accounts being affected by the transaction. The next column is the Ledger Folio (LF). We know that after the transactions are recorded in Journal, next they are transferred to Ledger. So LF is the page on which a transaction is classified in the ledger. It is for reference sake and is filled up at the time of preparing ledger. In the next two columns i.e. debit (Dr.) and credit (Cr.) we note down the dual aspect of each transaction.

8.6.2 Ledger : Classifying Transactions

This is the second stage in the accounting process in which we *classify the transactions into various different accounts*. Now the question arises why do we need to classify accounts? We know that during a month we write down all the transactions taking place in the Journal. So if we want to know how much expenses we have incurred on stationary or the total amount of fees collected during the month, or the amount of cash available with the school, this information is not there in the Journal.

So in Ledger all transactions pertaining to a single account are accumulated at one place. For example, all transactions pertaining to cash will be shown in the Cash A/c, all transactions pertaining to stationary will be shown in one account. The format of an account is given as under:

Capital A/c or Proprietor's Funds A/c

Dr.				Cr.			
DATE	PARTICULARS	J.F.	AMOUNT	DATE	PARTICULARS	J.F.	AMOUNT

The account has two sides- left hand side is known as Debit (Dr.) side and right hand side is the Credit (Cr.) side. This is also known as T-shaped Account. There are similar columns on both Dr and Cr side. First is the 'Date' in which we write down the date of the transaction as recorded in Journal and the vouchers. In the 'Particulars' column, the names of those accounts are written which give Dr or Cr to this particular account. The name of the account in the Dr side is preceded by writing 'To' and the Cr side by 'By'. In J.F. (Journal Folio), we write down the folio or page number of Journal from where the transaction is noted. And we write down the folio of Ledger in the Journal also. You would recall that there was a LF column in Journal. In the last column we write down the value of the transaction. Let us discuss this with the help of an example:

Example 1:

Prepare the Journal and post the entries into the Ledger for the following transactions:

Jan 4: Received cash on account of fees- Rs. 5,00,000

Jan 10: Furniture purchased from X Rs. 5,00,000

Jan 12: Equipment purchased Rs. 3,00,000

The above transactions will be shown in the Journal as:

Journal
(in the books of _____)

J.V.No.	DATE	PARTICULARS	L.F.	AMOUNT (Dr.)	AMOUNT (Cr.)
	2005 Jan 4	Cash A/c Dr. To Fees A/c (Being fees received in Cash)		5,00,000	5,00,000
	Jan 10	Furniture A/c Dr. To X (Being furniture purchased from X)		5,00,000	5,00,000
	Jan 12	Equipment A/c Dr. To Cash A/c (Being Equipment purchased for cash)		3,00,000	3,00,000

Here, in *the first transaction*, the two accounts involved are *Cash A/c* and *Fees A/c*. So, # Cash A/c is debited (since cash is coming in and the rule is debit what comes in) and # # Fees A/c is credited (since fees is income and rule says credit all incomes and gains) **NOTE:** After the entry is written, we write the narration to describe the entry in brackets as shown after each and every entry.

In the *second transaction*, the two accounts affected are the *Furniture A/c* and *X (creditor) A/c*. Since the name of the creditor is given so we presume that furniture has been bought on credit; otherwise the affected account would have been the

cash A/c; which is not the case here. So, here Furniture A/c is debited (since it is coming in; and we have to debit what comes in) and X's A/c is credited (since he is the giver and we have to credit the giver)

In the *third transaction*, similarly equipment has been bought, but for cash. So the affected accounts are *Cash A/c* and the *Equipment A/c*. so we have debited the Equipment A/c and Credited the Cash A/c.

POSTING IN THE LEDGER

In order to show the above transactions in Ledger we will have to open all affected accounts as shown below:

Cash A/c

Dr.			Cr.		
Date	Particulars	Amount	Date	Particulars	Amount
<u>2005</u> Jan 4	To Fees A/c	5,00,000	<u>2005</u> Jan 12	By Equipment A/c	3,00,000
				By Balance c/d (Closing Balance)	2,00,000
			Jan 31		
		5,00,000			5,00,000

Fee A/c

Dr.			Cr.		
Date	Particulars	Amount	Date	Particulars	Amount
<u>2005</u> Jan 31	To Balance c/d	5,00,000	<u>2005</u> Jan 4	By Cash A/c	5,00,000
					5,00,000
		5,00,000			

Equipment A/c

Accounting and Auditing

Dr.

Cr.

Date	Particulars	Amount	Date	Particulars	Amount
<u>2005</u>			<u>2005</u>		
Jan 12	To Cash A/c	3,00,000	Jan 31	By Balance c/d	3,00,000
					3,00,000
		3,00,000			

Furniture A/c

Dr.

Cr.

Date	Particulars	Amount	Date	Particulars	Amount
<u>2005</u>			<u>2005</u>		
Jan 10	To X A/c	5,00,000	Jan 31	By Balance c/d	5,00,000
					5,00,000
		5,00,000			

X A/c

Dr.

Cr.

Date	Particulars	Amount	Date	Particulars	Amount
<u>2005</u>			<u>2005</u>		
Jan 31	To Balance c/d	5,00,000	Jan 10	By Furniture t A/c	5,00,000
					5,00,000
		5,00,000			

Therefore, we can see that both the aspects of a transaction are shown in their respective accounts in the ledger. Ms Nair pointed out that a very important thing which is to be done is to **tally both the sides of each account**. The difference is known as the closing balance of the account and is carried down (c/d) to the next month or year by writing "To balance c/d" in case of credit balance and "By balance c/d" in case of debit balance.

The balances which are carried forward are shown in the next month accounts as opening balances in the debit side (To balance b/d) and in the credit side as (By balance b/d) as the case may be. In this way the balances of all accounts are calculated and then we prepare the Trial Balance.

8.6.3 Trial Balance

Once the process of posting to all ledger accounts is complete and the balances are calculated, these balances can be used to prepare the financial statements. But before doing that the correctness of the ledger accounts has to be ensured. In order to ensure the correctness of the accounts, we prepare the 'Trial Balance'.

Trial Balance is basically a list of names and balances of all accounts appearing in the ledger. We know that all transactions have dual aspect i.e. equal amounts of debits and credits and these same amounts are posted in the ledger so, it becomes imperative that the total of all debits is equal to total of all credits. Therefore, the total of all debits and credits in a trial balance tallies. Thus, we can conclude that **Trial Balance is a statement of balances of all ledger accounts prepared to verify the correctness of ledger accounts.**

The format of Trial Balance with the balances of above given ledger balances are shown below:

Trial Balance

Of _____ at 31st Jan., 2005

Account Heads	L.F.	Debit	Credit
1. Cash A/c		2,00,000	
2. Fees A/c			5,00,000
3. Equipment A/c		3,00,000	
4. Furniture A/c		5,00,000	
5. X A/c			5,00,000
		10,00,000	10,00,000

So we can see that both the sides in this trial balance is tallying. Therefore, we can conclude that our accounts are correct.

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

8) Is Trial Balance final proof of correctness of Accounts? Explain.

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9) Enumerate the steps of an accounting cycle.

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No, not all the errors can be detected with Trial Balance. There are certain errors which if committed cannot be seen in the Trial Balance. They are briefly discussed below:

1. **Error of Principle**: There are the errors in which some basic principle or rule of accounting is violated e. g. purchase of assets is shown as revenue expenditure.
2. **Error of Omission**: When one or more transactions are not recorded fully or partially in the books of accounts.
3. **Error of Commission**: such errors consist of entries of the transactions in a wrong account of the same class e.g. posting of an entry in the account of A.N. Suri instead of S.N. Suri's account.
4. **Compensatory Errors**: these errors are self-balancing and do not affect the balancing of Trial Balance e.g. Praveen's account is debited by Rs. 2,500 instead of Rs. 2,700 and Atul's account is debited by Rs. 3,200 instead of Rs 3,000.

Now, let us take up a comprehensive example to understand the the whole process of Journal, Ledger and Trial Balance:

Example 2:

Journalize the following transactions and prepare Ledger Accounts with closing balance on 30th April, 2006. Also prepare the Trial Balance from the Ledger Accounts:

- April 1: Cash invested by Proprietor Rs. 20,00,000
- April 1: Building purchased for Rs. 12,00,000
- April 2: Stationery purchased for Rs. 25,000.
- April 3: Furniture purchased for Rs. 5,00,000
- April 5: Cash received on account of fees Rs. 5,00,000
- April 10: Equipment purchased from X for Rs. 3,00,000
- April 12: Loan from Bank taken Rs. 20,00,000.

April 20: Library books purchased for Rs. 5,00,000, payment made by cheque.

April 25: Withdrawn money for personal use from bank Rs. 50,000

April 26: Purchased a car for institute's use Rs. 2,00,000

April 27: Salaries paid to staff Rs. 80,000.

April 27: Payment made to X Rs. 2,95,000 in full settlement.

April 28: Received Sports fee Rs. 85,000

April 28: Received donations Rs. 2,00,000

April 29: Personal telephone bill paid for proprietor Rs. 1,500.

Now let us prepare the Journal, Ledger and Trial Balance out of these transactions:

Journal

(in the books of _____)

J.V.No	DATE	PARTICULARS	L.F.	AMOUNT (Dr)	AMOUNT (Cr)
	2006 April 1	Cash A/c Dr. To Proprietor's A/c (Being capital bought by the proprietor in cash)		20,00,000	20,00,000
	April 1	Building A/c Dr. To Cash A/c (Being building bought for cash)		12,00,000	12,00,000
	April 2	Stationary A/c Dr. To Cash A/c (Being stationary purchased for cash)		25,000	25,000
	April 3	Furniture A/c Dr. To Cash A/c (Being furniture bought for cash)		5,00,000	5,00,000
	April 5	Cash A/c Dr. To Fees A/c (Being cash received on account of fees)		5,00,000	5,00,000
	April 10	Equipment A/c Dr. To X (Being equipment purchased on credit from X)		3,00,000	3,00,000
	April 12	Bank A/c Dr. To Bank Loan A/c (Being loan taken from bank)		20,00,000	20,00,000

April 20	Library Books Dr To Bank A/c (Being books purchased for library and payment made by cheque)	5,00,000	5,00,000
April 25	Drawings A/c Dr To Bank A/c (Being cash withdrawn from bank for personal use)	50,000	50,000
April 26	Car A/c Dr To Cash A/c (Being car purchased for office use)	2,00,000	2,00,000
April 27	Salaries A/c Dr To Cash A/c (Being salaries paid to employees in cash)	80,000	80,000
April 27	X Dr To Cash A/c To Discount A/c (Being payment made to X in full settlement and discount received)	3,00,000	2,95,000 5,000
April 28	Cash A/c Dr To Sports Fee A/c (Being Sports Fee received)	85,000	85,000
April 28	Cash A/c Dr To Donation A/c (Being donation received in cash)	2,00,000	2,00,000
April 29	Drawings A/c Dr To Cash A/c (Being personal telephone bill paid out of institute's fund)	1,500	1,500
April 30	Bank A/c Dr To Cash A/c (Being Donation amount deposited in Bank)	2,00,000	2,00,000

Cash A/c

Dr.			Cr.		
Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 1	To Proprietor's Capital	20,00,000	April 1	By Building A/c	12,00,000
April 5	To Fees A/c	5,00,000	April 2	By Stationary A/c	25,000
April 28	To Sports fees A/c	85,000	April 3	By Furniture A/c	5,00,000
April 28	To Donations A/c	2,00,000	April 26	By Car A/c	2,00,000
			April 27	By Salaries A/c	80,000
			April 27	By X	2,95,000
			April 29	By Drawings A/c	1,500
			April 30	By Bank A/c	2,00,000
			April 30	<i>By Balance c/d (closing balance)</i>	<i>2,83,500</i>
		27,85,000			27,85,000

Bank A/c

Dr.			Cr.		
Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 12	To Bank Loan	20,00,000	April 20	By Library Books	5,00,000
April 30	To Cash A/c	2,00,000	April 25	By Drawings A/c	50,000
			<i>April 30</i>	<i>By Balance c/d (closing balance)</i>	<i>16,50,000</i>
		22,00,000			22,00,000

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	To Balance c/d (closing balance)	20,00,000	April 1	By Cash A/c	20,00,000
		20,00,000			20,00,000

Dr. Building A/c

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 1	To Cash A/c	12,00,000	April 30	By Balance c/d	12,00,000
		12,00,000			12,00,000

Dr. Stationary A/c

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 2	To Cash A/c	25,000	April 30	By Balance c/d	25,000
		25,000			25,000

Dr. Furniture A/c

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 3	To Cash A/c	5,00,000	April 30	By Balance c/d	5,00,000
		5,00,000			5,00,000

Dr. Fees A/c

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	To Balance c/d	5,00,000	April 5	By Cash A/c	5,00,000
		5,00,000			5,00,000

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 10	To X	3,00,000	April 30	By Balance c/d	3,00,000
		3,00,000			3,00,000

X A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 27	To Cash A/c	2,95,000	April 10	By Equipment A/c	3,00,000
	To Discount A/c	5,000			
		3,00,000			3,00,000

Bank Loan A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	To Balance c/d	20,00,000	April 12	By Bank A/c	20,00,000
		20,00,000			20,00,000

Library Books A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 20	To Bank A/c	5,00,000	April 30	By Balance c/d	5,00,000
		5,00,000			5,00,000

Drawings A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 25	To Bank A/c	50,000	April 30	By Balance c/d	51,500
April 29	To Cash A/c	1,500			
		51,500			51,500

Car A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 26	To Cash A/c	2,00,000	April 30	By Balance c/d	2,00,000
		2,00,000			2,00,000

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 27	To Cash A/c	80,000	April 30	<i>By Income and Expenditure A/c</i>	80,000
		80,000			80,000

Discount A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	<i>To Income & Expenditure A/c</i>	5,000	April 27	By X A/c	5,000
		5,000			5,000

Sports Fee A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	<i>To Income & Expenditure A/c</i>	85,000	April 28	By Cash A/c	85,000
		85,000			85,000

Donation A/c

Dr.

Cr.

Date 2005	Particulars	Amount	Date 2005	Particulars	Amount
April 30	<i>To Income & Expenditure A/c</i>	2,00,000	April 28	By Cash A/c	2,00,000
		2,00,000			2,00,000

NOTE: The balances of the Salaries A/c, Discount A/c, Sports Fee A/c and Donation A/c have been transferred to the Income and Expenditure A/c as these are *items of revenue incomes and expenditure* for the period. So these balances are not carried forward to the next accounting period; they are taken to the Income and Expenditure A/c from which we come to know the total income (surplus) or deficit of the institution for the period.

TRIAL BALANCE

(As on 30th April, 2005)

Account Heads	L.F.	Dr.	Cr.
Proprietor's Funds			20,00,000
Bank Loan A/c			20,00,000
Buildings A/c		12,00,000	
Furniture A/c		5,00,000	
Equipment A/c		3,00,000	
Library Books A/c		5,00,000	
Stationary A/c		25,000	
Fee A/c			5,00,000
X A/c		-----	-----
Drawings A/c		51,500	
Car A/c		2,00,000	
Donation A/c			2,00,000
Salaries A/c		80,000	
Discount A/c			5,000
Sports Fee A/c			85,000
Bank A/c		16,50,000	
Cash A/c		2,83,500	
		47,90,000	47,90,000

Thus, we can see that after taking the balances of all accounts in the Trial Balance, the total of both the sides tallied.

8.7 FINANCIAL STATEMENTS TO BE PREPARED AT THE END OF THE YEAR

After the preparation of the Trial Balance, the final stage in the accounting process is the preparation of Financial Statements at the end of accounting period. Although educational institutions are non-profit organisations (NPOs) but still the organizers, contributors and the society at large would like to know the result of their activities. So these organizations do not find out profit or loss of their operations. In order to show their various items of incomes and expenditures, the NPOs basically need to prepare these *financial statements* at the end of the financial year to know the surplus (excess of income over expenditure) or deficit (excess of expenditure over income). The institutions prepare the following financial statements:

1. Receipts and Payments A/c
2. Income and Expenditure A/c
3. Balance Sheet

8.7.1 Receipts and Payments A/c

A Receipts and Payment Account is a summary of Cash Book or Cash Account. It is prepared to present the result of the organization's cash position. This account is a **Real Account**. Hence on the debit side all receipts (whether in cash or cheque) are recorded and all payments (Cash or cheque) are recorded on the credit side. It starts with the opening cash and bank balances on the debit side; and ends with their closing balances on the credit side. If there is a bank overdraft in the beginning of the accounting period, it appears as the first item on the credit side. Another very important point to be noted is that no distinction is made between Capital and Revenue Receipts and Payments. All receipts and payments made during the year are shown, irrespective of the fact whether they are related to the present period or not. For example, if we received a payment in advance which relates to the next accounting period, it will be shown in the account. Similarly, if a payment pertaining to the previous year is received in the current period, it will be shown. So ***all receipts (by cash or cheque); of capital and revenue nature; pertaining to past, present and future periods are shown in the Receipts and Payments Account.*** The pro-forma is given below:

Receipts and Payments A/c

RECEIPTS	AMOUNT	PAYMENTS	AMOUNT
<u>Balance b/d (opening):</u>		<u>Balance b/d (Bank Overdraft) (opening Balance)</u>	
Cash in Hand			
Cash at Bank			
<u>Capital Receipts (for past, present & future periods):</u>		<u>Capital Payments (for past, present & future needs):</u>	
Legacies		Building- purchased or constructed	
Sale of office furniture		Sports equipment	
Sale of equipment		Cost of Leasehold Land	
Donations received for specific purposes eg.		Bank Loan	
Buildings, prizes etc *		Purchase of any asset	
Sale of investments		<u>Revenue Payments (for past, present & future periods):</u>	
Interest on funds		Prizes paid	
<u>Revenue Receipts (for past, present & future periods):</u>		Entertainment expenses	
Government grants **		Printing and stationary	
Entrance fees		Newspapers & Magazines	
General donations *		Repairs	
Proceeds from fairs, entertainment		Postages	
Sale of old newspaper, magazines		Insurance, rent, salaries	
Miscellaneous receipts		Advertisement	
<u>Balance c/d (Bank Overdraft) (closing balance)</u>		Audit fee	
		Telephone & electricity charges	
		Garden maintenance	
		Municipal taxes	
		Charity	
		Printing of diaries, magazine, newsletter etc.	
		Bank overdraft (adjustment)	
		Drawings	
		<u>Balance c/d</u>	
		<u>Cash in Hand</u>	
		<u>Cash at Bank</u>	

Note:

- i) **Donation:** it is a sort of gift in cash or in kind received from some existing person, firm or company. It appears on the Receipts side of Receipts and Payments Account, if received in cash. They can be for a specific purpose or for general purpose. If the donation is for a specific purpose, it is capitalized and is shown in the liabilities side of Balance Sheet. If the donation is general, then it is treated as revenue income as they are generally received every year. So this is shown as income in the Income and Expenditure Account.
- ii) **Government Grants** may be of revenue nature if such grants are received regularly and are of recurring nature.

8.7.2 Income and Expenditure A/c

It is prepared to find out the **Surplus** (excess of income over expenditure) or **Deficit** (excess of expenditure over income). It is a **nominal account**. The debit side of this account is known as the Expenditure side and credit side is known as the Income side. The balance of this account – surplus or deficit – is transferred to the Balance Sheet. Surplus is added to the Capital Fund and deficit is deducted from the Capital Fund.

A very important point to be kept in mind is that all **revenue** items of **incomes** and **expenditures** are shown in this account. Capital receipts and capital expenditures are excluded for example if any fixed asset has been purchased, or any amount received from sale of investments or any other fixed asset are not shown in this account as these are not of recurring nature. Another, very important point is that only those items are shown **which pertain the current accounting period**. So any amount received or paid which pertains to the preceding or succeeding accounting period is not shown. Also we need to keep in mind that any income or expenditure which is accrued (any outstanding payment or income) in the present accounting period is shown as it pertains to the current year. The pro-forma is given below:

Income and Expenditure A/c
(For the year ending on _____)

EXPENDITURE	AMOUNT	INCOME	AMOUNT
Any expense (like salaries) Total paid: <u>Add:</u> outstanding at the end <u>Less:</u> outstanding in the beginning <u>Add:</u> advance paid in the previous year <u>Less:</u> advance paid for the current year Salaries for the year Expenses on consumables: Opening stock <u>Add:</u> purchases during the year <u>Less:</u> Creditors in the beginning		Any Income (eg fees): Total amount received <u>Add:</u> outstanding at the end <u>Less:</u> outstanding in the beginning <u>Add:</u> advance received last year <u>Less:</u> advance received this year Current income Government grant Profit on sale of an asset (sale price – book value) Other revenue receipts Donations (general) Income on specific items	

<u>Add:</u> Creditors at the end		Deficit (excess of	
<u>Less:</u> advance payments in the current year		expenditure over income)	
<u>Add:</u> advance payments in the previous year			
<u>Less:</u> closing stock			
Value actually used			
Loss on sale of an asset (Book value-sale price)			
Other expenses and losses			
Depreciation			
Surplus (excess of income over expenditure)			

8.7.3 Balance Sheet

It is a statement which shows the financial position of an organisation on a specific date. That is why it is prepared on a specific date and does not represent the whole year. The Balance Sheet provides information on nature and book value of assets, nature and amount of liabilities, the amount of proprietor's funds and its liquidity position. It has two main columns i.e. Assets and Liabilities. Under the Assets column we show all the assets of the organisation like Land, Building, Machinery, Equipment, Furniture, Stock of various items, Cash in hand and Cash at Bank. In the Liabilities side, we show different Liabilities of the organisation like the Proprietor's Fund, Capital Fund, any Legacy or Special Fund, Reserves and Surpluses, and Liabilities towards outside parties like creditors, any debt taken from bank or individuals etc. The pro-forma is given below:

Balance Sheet

(as on _____)

LIABILITIES	AMOUNT	ASSETS	AMOUNT
Capital Fund (Proprietors' Capital)		Assets (Book Value)	
Add: Surplus		Last balance	
Less: Deficit		Add: purchased during the year	
Capital Incomes		Less: book value of the asset sold	
Legacies		Less: depreciation	
Special Donations/Fund:		Stock of consumable materials	
Creditors		Outstanding income	
Any outstanding expenditure (eg salaries)		Cash at Bank	
Bank overdraft		Cash in Hand	

Example 3:

Now let us discuss a practical case. Below is the Trial Balance of Shri Venkateshwar Educational Society. Prepare the Income and Expenditure Account for the year ending 31st March, 2005 and a Balance Sheet as on that date.

TRIAL BALANCE

DEBIT BALANCES	AMOUNT	CREDIT BALANCES	AMOUNT
Building	2,50,000	Admission fees	5,000
Furniture	40,000	Tuition Fee	2,00,000
Library Books	60,000	Creditors for supplies	6,000
Investments @ 9%	2,00,000	Rent for the school hall	4,000
Salaries	2,00,000	Misc. Receipts	12,000
Stationary	15,000	Government Grant	1,40,000
General Expenses	8,000	Capital Fund	4,00,000
Sports Expenses	6,000	Donation for Library Books	25,000
Cash at Bank	20,000	Sale of old furniture	8,000
Cash in Hand	1,000		
	8,00,000		8,00,000

Additional Information:

Fees yet to be received for the year are Rs. 10,000. Salaries yet to be paid amount to Rs. 12,000. Furniture costing Rs. 15,000 was purchased on 1-10-2004. The Book Value of the furniture sold was Rs. 20,000 on 1-4-2004. Depreciation is to be charged @ 10% p.a. on Furniture, 15% on Library Books and 5% on Building. Give working Notes.

Shri Venkateshwar Educational Society

INCOME AND EXPENDITURE A/C

(for the year ended 31st March, 2005)

EXPENDITURE	AMOUNT	INCOME	AMOUNT
Loss on sale of Furniture	12,000	Admission Fees	5,000
Salaries 2,00,000		Tuition Fees 2,00,000	
Add: outstanding 12,000	2,12,000	Add: outstanding 10,000	2,10,000
Stationary	15,000	Rent for school hall	4,000
General Expenses	8,000	Miscellaneous receipts	12,000
Depreciation:		Government Grant	1,40,000
Furniture	1,250		
Building	12,500		
Library Books	9,000		
Sports Expenses	6,000	Interest accrued on investments	18,000
Surplus	1,13,250		
	3,89,000		3,89,000

BALANCE SHEET

Accounting and Auditing

(As on 31st March, 2005)

LIABILITIES	AMOUNT	ASSETS	AMOUNT
Creditors for supplies	6,000	Buildings 2,50,000	
		Less: Depreciation 12,500	2,37,500
Outstanding salaries	12,000	Furniture 40,000	
		Less: sold 20,000	
		Less: Depreciation 1,250	18,750
Donation for Library Books	25,000	Accrued Fees	10,000
Capital Fund 4,00,000		Library Books 60,000	
Add: Surplus 1,13,250	5,13,250	Less: Depreciation 9,000	51,000
		Investments @ 9%	2,00,000
		Interest accrued	18,000
		Cash at Bank	20,000
		Cash in Hand	1,000
	5,56,250		5,56,250

Working Notes:

Admission Fees is a regular income of the school.

Depreciation has been calculated on furniture assuming that it was sold on 1st April, 2004.

Book Value on 31st march, 2004 40,000

Less: Book Value sold 20,000

20,000

Depreciation on Rs. 5,000 for one year 500

Depreciation on Rs. 15,000 for + 750

6 months (Oct. - March)

1250

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

10) State whether the following statements are true or false:

1. Revenue receipts are not shown in the Receipts in Payments Account
2. Capital receipts are shown in Income and Expenditure Account
3. Items of non-recurring nature are shown in Balance Sheet

11) What are the receipts and payment account ?

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8.8 AUDITING- CONCEPT

Till now we have discussed the procedure of maintenance of accounts. Once the process of accounting ends, the process of auditing starts. An auditor examines and verifies the items therein with the help of relevant documentary evidence and explanations and information given to him. Or we can say that the auditor critically analyses the accounts and financial statements prepared by the accountant. The Institute of Chartered Accountants of India (ICAI) has defined auditing in the following words.

“Auditing is a systematic and independent examination of data, statements, records, operations and performance (financial or otherwise) of an enterprise for a stated purpose. In any auditing situation, the auditor perceives and recognizes the proposition before him for examination, collects evidence, evaluates the same and on this basis, formulates his judgment which is communicated through his audit report.”

The key points in the definition are discussed as under:

- **Systematic:** An audit has to be carefully planned and sequenced logically.
- **Independent:** The auditor while formulating and expressing his opinion should not be susceptible to any influence from client or anybody else.
- **Data, statements, records, operations and performance:** This phrase indicates the scope of audit. It extends from examination of books to review of vouchers to performance connected to non-financial areas also.
- **Stated purpose:** The stated purpose should be clearly defined. For example, the stated purpose of Environment audit is to examine and report on verifiable quantitative and qualitative information in the area of environmental concerns.
- **Perceives and recognizes the propositions before him for examination:** The auditor must know ‘what he/she has to prove’.
- **Collects evidence, evaluates the same:** The auditor has to take into account all kinds of evidences like books of accounts, tax returns, direct confirmation, departmental budgets etc.
- **Formulates his judgment which is communicated through his audit report:** The opinion of the auditor is communicated through an audit report which is made depending upon the type of audit, statutory requirements and purpose of audit.

8.9 OBJECTIVES OF AUDIT

The objective of a financial audit is to determine whether the financial statements are prepared in accordance with generally accepted accounting principles (GAAP).

The management of an organization is responsible for preparing the financial statements. The auditor is responsible for rendering an opinion on the fairness of those financial statements based on his or her audit. The two broad objectives of audit are discussed below:

1. **Expression of opinion about the truthfulness and fairness of financial statements:** The primary objective of auditing is expression of opinion that the financial statements of an enterprise do show true and fair view of its financial position and earnings. So the auditor has to ensure that these statements comply with:
 - (i) recognized accounting principles which have been consistently applied.
 - (ii) relevant legislation and
 - (iii) are correctly extracted from books and records.
2. **Detection and Prevention of Error and Frauds:** An incidental but very important objective of audit is detection and prevention of frauds and errors. For an auditor it is very important to distinguish between error and fraud which is briefly described below with the help of the following diagram:

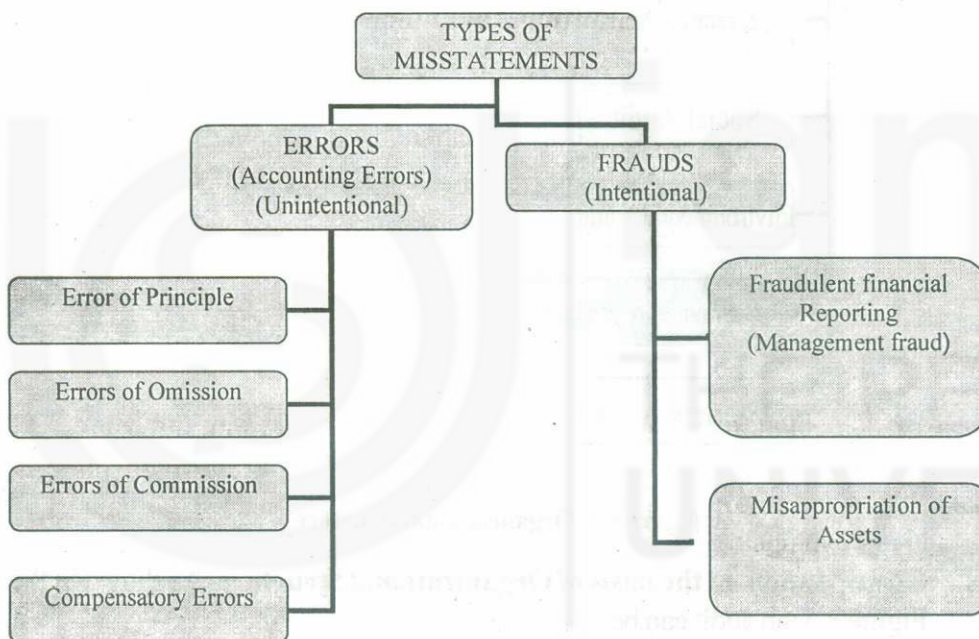


Figure 8.2: Types of Errors

As shown in the Figure 8.2, the auditor's job is detection of various errors and frauds, as both results in misstatement of financial statements. Though the responsibility of the auditor is same in both the situations, however distinction is important in practice because fraud raises doubt about the integrity of management and those charged with governance.

8.10 TYPES OF AUDIT

Auditing can be classified into different types as follows:

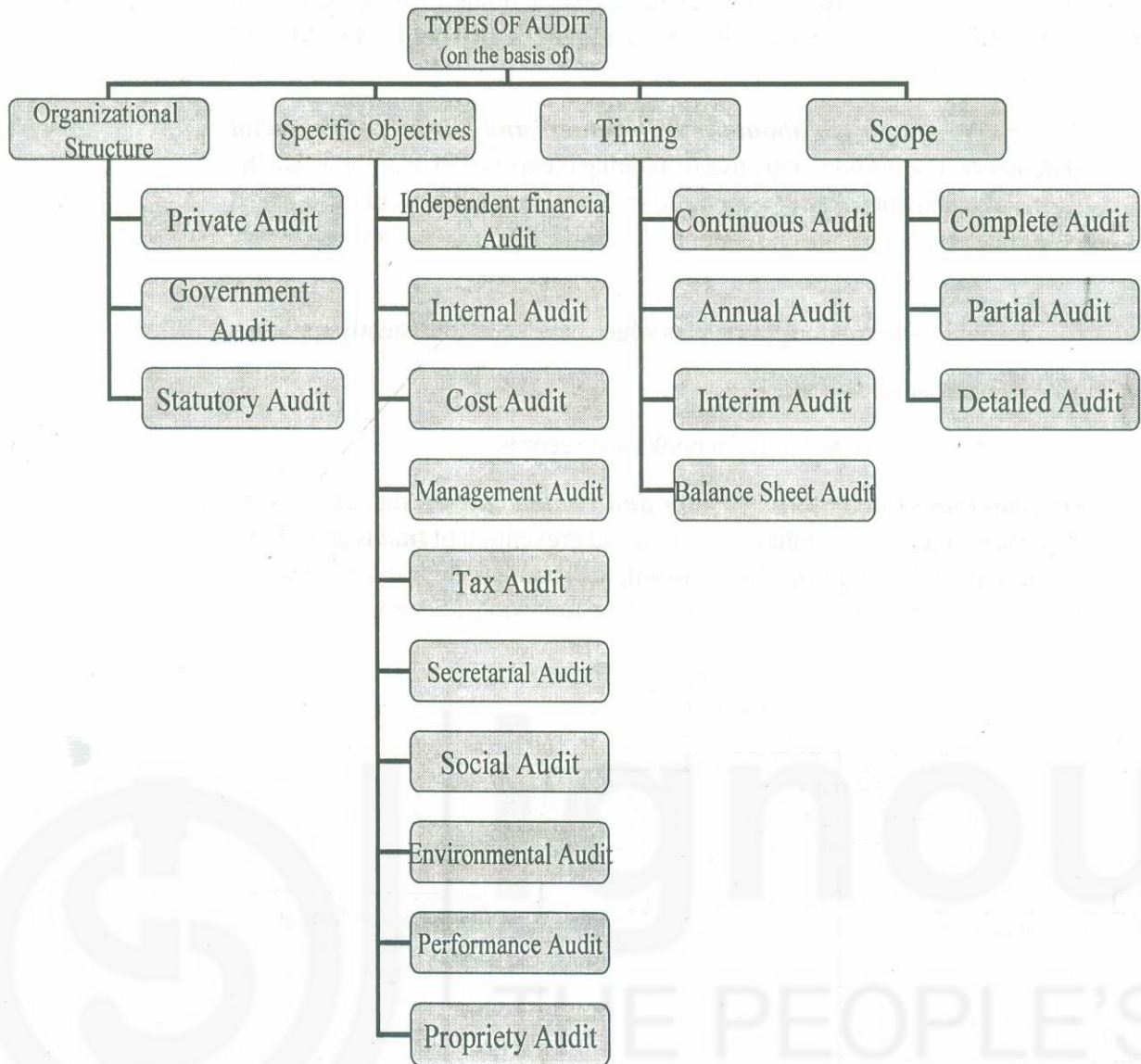


Figure 8.3: Organisational structure

1. **Classification on the basis of Organizational Structure-** As shown in the Figure 8.3, an audit can be:
 - (i) **Private Audit-** it is carried not to satisfy any statutory requirement but at the initiative of the management. It is generally carried out by sole, proprietors, partnership firms, individuals and non-profit organisations.
 - (ii) **Government Audit:** It is the audit of commercial accounts maintained by public enterprises such as departmental undertakings, statutory corporations and government companies. It is basically a control measure for public accounting of government funds.
 - (iii) **Statutory Audit:** Audit which is made compulsory under any statute is Statutory Audit. Various acts like the Companies Act 1956, The Insurance Act 1938, the Co-operative Societies Act of various states passed various laws for different organisations regarding various auditing procedures.
2. **Classification on the basis of Specific Objectives:** Different types of audit can be carried to meet specific objectives as explained below:

- (i) **Independent Financial Audit:** Independent Financial Audit has been made compulsory by different regulatory authorities under different Acts. Most of the educational institutions have to go for it by compulsion. It is carried out by professionally qualified auditors and the purpose is to ascertain the truthfulness and fairness of the financial statements. At the end the auditor submits his report which is a very useful document for the organisation for meeting different requirements.
- (ii) **Internal Audit:** Internal audit is generally carried out by the employees of an institution appointed by management to review financial and non-financial operations. The objective of internal audit is to suggest improvement to the function of the entity and add value to and strengthen the overall governance mechanism of the entity including strategic risk management and internal control systems. Thus it is more of a managerial control mechanism to ensure that- (a) financial and other types of information is reliably recorded, (b) the valuation of assets of an institute is done as per the policies and plans of the management and as per the accounting norms, (c) the resources of the institution are used in the most efficient manner. It is generally carried out throughout the year.
- (iii) **Cost Audit, Management Audit, Tax Audit, Secretarial Audit, Performance Audit and Propriety Audit:** These audits are conducted for meeting specific needs. Cost Auditing pertains to correctness of cost accounts. Management Audit is for examining and reviewing the various plans, policies and actions of management on certain specified standards. Tax Audit is done to assess the correctness of calculation of Income and other taxes under the provisions of different Acts. The objective of Secretarial Audit is to ensure that full and adequate compliance of various legal requirements has been established in the institution. Performance audit is concerned with valuation of performance against set standards and Propriety audit ensures that whether the actions and decisions of the institution are in public interest or not.
- (iv) **Social Audit and Environment Audit:** Awareness of social responsibility of institutions has led organisations to go in for social audit. It is conducted on four major areas of social performance- (a) *Community Development*, (b) *Human Resource Development*, (c) *Physical contribution and environmental contribution* and (d) *Product or Service contribution*. If we see around us we can see that in one way or the other all institution try to contribute towards these social causes. In the same way, Environmental Audit is a management tool comprising a systematic, periodic and objective evaluation of how well organisation, management and equipment are performing to *safeguard the environment*. It is concerned with assessing whether institutions policies meet regulatory requirements or not.

3. Classification on the basis of time: Depending upon the time at which the audit is carried out, the different types are:

- (i) **Continuous Audit:** According to R.C. Williams "A continuous is one where the auditor or his staff is constantly engaged in checking the accounts during the whole period or where the auditor or his staff attends at regular or irregular intervals during the period." It has the advantage of early detection of frauds and errors plus the auditor gets knowledge of all technical details which leads to efficiency of the auditors and acts as moral check on the staff.

- (ii) **Annual Audit:** Audit which is carried out once only at the end of an accounting period once the books of accounts are closed is annual audit. The work of auditing is completed in a single continuous session. It is effective for small concerns.
 - (iii) **Interim Audit:** Audit conducted between two annual audits is called interim audit. It is always carried out for a specific purpose and does not enjoy a statutory status.
 - (iv) **Balance Sheet Audit:** It is a limited audit in which all the Balance Sheet items are verified.
4. **Classification on the basis of scope of audit:** There can be complete, partial or detailed audit on the basis of scope of audit. These are briefly described below:
- (i) **Complete Audit:** In this the auditor is appointed to check all transactions and books of accounts with the help of relevant vouchers, documents, correspondence etc. It is not feasible or practicable.
 - (ii) **Partial Audit:** When the audit is conducted on some of the records and books or a part of books for whole or part of the period, it is called partial audit.
 - (iii) **Detailed Audit:** Audit which starts with the books of prime entry and ends with the Balance Sheet. The checking sequence is arranged in order of recording the transactions in the books of accounts.

Therefore, an educational institution has to go in for statutory, independent financial, detailed audit (in majority of cases) on a continuous or annual basis as per the requirement of the management and in conformation of different regulatory authorities.

8.11 AUDIT REPORT

After the auditing has been carried out by the auditor, he/ she prepares a report communicating his/her opinion on the truthfulness and fairness of financial statements. The auditor's report may be unqualified, unqualified with an 'emphasis of matter', qualified or an adverse report commenting on the (a) weakness or strengths of accounting system in that institution, (b) inadequacies in the financial policies and practices, (c) deficiency in the financial control system (d) non-compliance with the accepted accounting practices. In response to the auditor's report the institution has to take the required corrective action maybe in the form of submitting further information, checking of figures, calculation, balances etc in Trial Balance, or going over the books of accounts in order to check for any fraud or errors that might have crept into the books advertently or inadvertently.

Check Your Progress

- Note :** a) Space is given below for writing your answers.
- b) Check your answers with those given at the end of this unit.

12) What are the two broad objectives of audit ?

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13) In to how many types audit is classified on the basis of time?

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14) Mention the functions of auditor.

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8.12 LET US SUM UP

The main point under discussion in this unit is the development or understanding of a concept of accounting and auditing of a school organization in a particular way . The accounting has certain rules, principles, and concepts, on the other hand auditing has to be carefully planned and sequenced logical activities. Actually both are the important part of an organisation. When the process of accounting ends, the process of auditing starts. Actually, accounting information is stand on two set of people- i.e. Internal and external . On the another way auditing can be categorised in a different way, but which types of auditing is required it depends on the particular institution and situation.

8.13 UNIT END ACTIVITIES

Select any educational institution. Study accounting and auditing statements of a financial year and analyse in the context of points given in the unit. Write a report highlighting on the advantages and disadvantages.

8.14 REFERENCES

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Monga, J.R.; Financial Accountng; Mayur Paperbacks;NOIDA; 2007-08

Mukherjee, Amitabha and Mohammed Hanif; Modern Accountancy; Tata Mc-Graw Hill Publishing Company; New Delhi; 2002

Jha, Aruna; Auditing; Taxmann Allied Services (P) Ltd.; New Delhi; 2007

8.15 ANSWERS TO CHECK YOUR PROGRESS

1. Partners, Managers and Investors, landers.
2. The meaning of GAAP is Generally Accepted Accounting Principles.
3. Ref. subsection 8.3
4. Ref. subsection 8.3

5. Ref. subsection 8.3
6. Ref. subsection 8.5
7. Capital expenditure is an expenditure which is incurred- (i) to buy a fixed asset. (ii) increase the useful life of fixed asset. (iii) increase the productivity (iv) making an asset usable or reusable. In revenue terms are those which are collected in usual course of business or regular basis e.g. fees collected, interest earned, commission received, donations received etc.
8. Ref. subsection 8.6.3
9. The steps in the accounting cycle
 1. Identify the Transaction
 2. Analyze the Transation
 3. Making entries in the Journal
 4. Posting to Ledger
 5. Preparation of Trial Balance
 6. Preparation of Financial Statements
10. Ref. Section Accounting
11. Ref. subsection 8.7.1
12. (i) Expression of opinion about the truthfulness and fairness of financial statements
(ii) Detection and prevention of Error and Fraud.
13.
 1. Continuous Audit
 2. Annual Audit
 3. Interim Audit
 4. Balance Sheet Audit
14. Ref. Subsection 8.11

UNIT 9 RESOURCE MOBILISATION IN EDUCATION

Structure

- 9.1 Introduction
- 9.2 Objectives
- 9.3 Taxonomy of Resource Mobilisation
- 9.4 Internal Resource Mobilisation
 - 9.4.1 Graduate Tax
 - 9.4.2 Education Cess
 - 9.4.3 Prarambhik Shiksha Kosh (PSK) in Elementary Education
 - 9.4.4 Community Resource Mobilisation
 - 9.4.5 Fees
 - 9.4.6 Principles of Resources Mobilisation Through Cost Recovery
 - 9.4.7 Other Sources
 - 9.4.8 New Approaches
- 9.5 External Resource for Education
- 9.6 Policy Options in Resource Mobilisation
- 9.7 Let Us Sum Up
- 9.8 Unit-End Activities
- 9.9 References
- 9.10 Answers to Check Your Progress

9.1 INTRODUCTION

The Rationale for Resource mobilisation

We all are aware of that investment in education yield high economic returns to the society. More importantly, there are a multitude of externalities associated with education, including positive effects on health, reduction in infant mortality rate, reduction in fertility rate, etc. All these benefits and externalities of education necessitates a positive approach to financing and mobilising resources for education, and underscores the need to step up the levels of government and non-government expenditure on education substantially.

As we know plenty and huge resources are required for quantitative expansion, qualitative improvement and for the maintenance of the education system. The requirements of the education systems are much higher than the levels of availability of resources. Hence, resource mobilisation can be from internal and external resources. Within the internal resources for education, resources mobilisation can be from both within the government and non-government resources. Government has been the major source of finances of education in India and also in many developed and developing countries. The non-governmental sources are marginal/limited, but gaining momentum since 1990s in the country and also across the globe.

All types of resources financial, material and human resources and through all possible sources viz., government, household, private sector, communities, international donors and agencies are being tapped under the current regimes of economic globalization. (Indeed), it is needless to say that, resource mobilisation is an important agenda/ aspects both nationally and internationally and across school and higher education as well.

9.2 OBJECTIVES

After going through this Unit you would be able to:

- describe the reasons for resource mobilisation in education;
- list various resources that can be mobilized for education;
- analyze the limitations of the non-governmental or external sources of mobilizing resources for education.

9.3 TAXONOMY OF RESOURCE MOBILISATION

Resource mobilisation can be broadly categorised into internal and external resources. Internal resource mobilisation means generating resources within the country, whereas external resource mobilisation indicates mobilisation of resources from outside the country. (The Figure 9.1 illustrates the taxonomy of resource mobilisation). Let us go for illustrating the taxonomy of resource mobilisation.

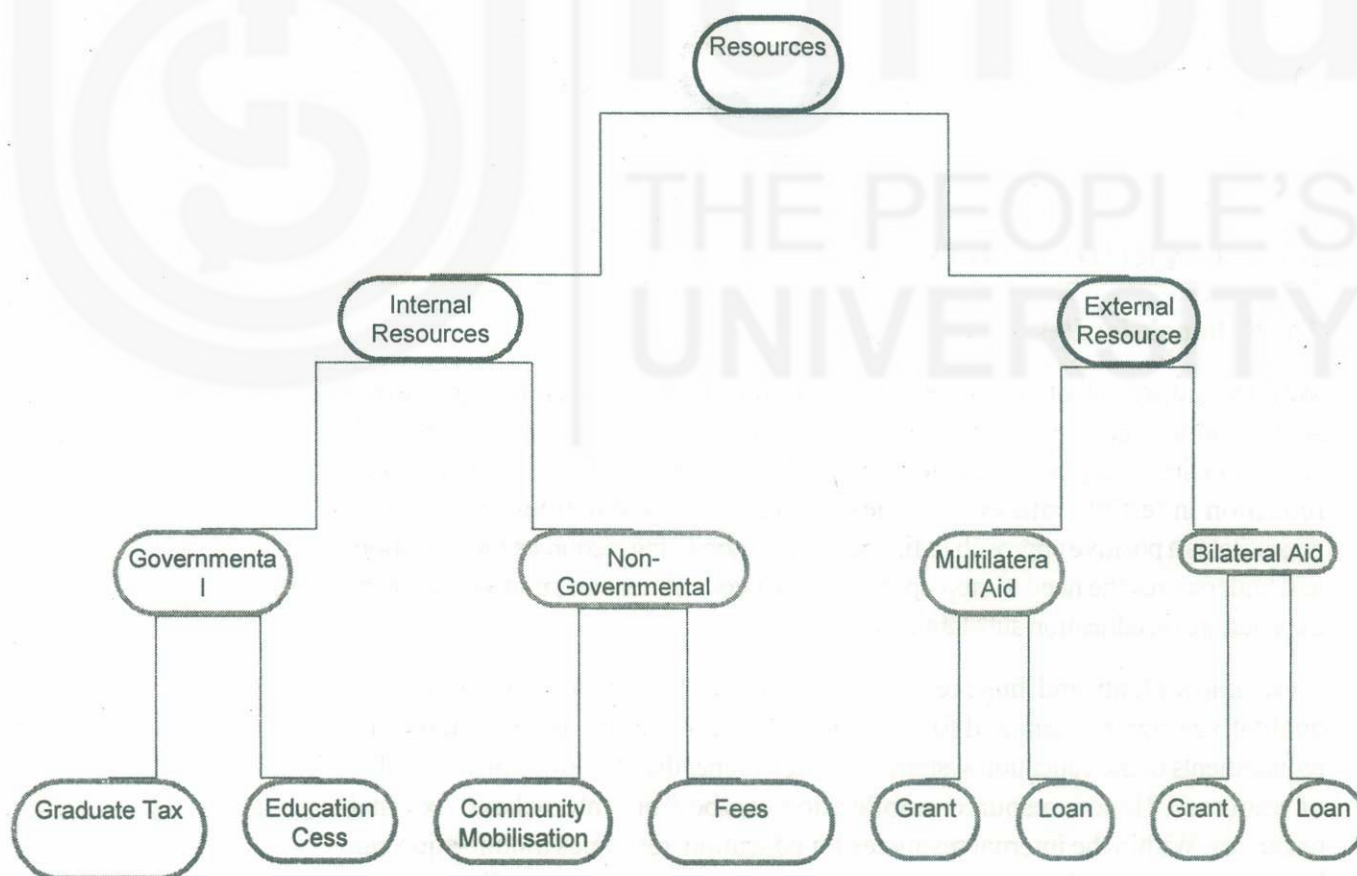


Figure 9.1: Taxonomy of Resource Mobilisation

You may be curious to know that how the resources mobilisation of education are working. Let us try to know the details -

Internal resource mobilisation means resources that are generated within the nation or domestic resource mobilisation for education. There are two broad sources of resource mobilisation at the domestic front such as **government** and **non-government** resources. For example in the context of an educational institution students fee, donations or grants received from the management revenue generated, for hiring the institution's building and other infrastructural facilities, etc. are non-governmental resource mobilisation.

- **Mobilising Governmental Resources for education:** Government Resources can be further categorized as the resources from the general pool of resources like the graduate tax which is specific or earmarked for education such as *education cess*.

9.4.1 Graduate tax

The common suggested measure is to recover the cost of higher education through the graduate tax. The graduate tax is an education specific tax levied on those who use educated manpower. The paradoxical situation in India is that while the expenditure on education is borne by the government, the products of the educational system are used by the public and private sectors. The educational sector in India provides manpower to the production sectors and they generate profits which are beneficial to the employers. However, employers seldom contribute to the education sector on a regular basis. There is, therefore, a strong case for levying a tax on every graduate who is employed in an organisation. An employer can be asked to pay an annual tax to the government for each graduate recruited. The amount of tax to be levied should be based on the cost of education at that particular level. The duration of the tax can be determined so as to recover the total cost of education.

This seems logical and hence a desirable proposition. The major drawback with the scheme is that it may work as a disincentive for many employers in recruiting University graduates; they may use lower level educated manpower as a substitute. This may exacerbate the already aggravated situation of unemployment of the better educated in India. The substitution possibilities may be lower in those organisations where the burden of taxation can be shifted to individual employees. Nevertheless taxing employers based on the type of manpower they use has a good rationale even if it leads to substitution.

9.4.2 Education Cess

Traditionally, education cess is an important additional, but small source of finance for education at the local level. Many states used to impose an education cess on land revenue in rural areas and on urban property in urban areas. An advantage with the education cess is that though it generates a small amount of resources, they are necessarily to be allocated to schools in the given area. They are earmarked that these resources cannot be used for some other purpose. These small resources are useful for implementing special programmes of quality improvement and innovation at the school level, as visualized and planned by school teachers. The Government of India has introduced an education cess since 2004 on all central taxes to finance the commitment to universalise access to quality basic education.

9.4.3 Prarambhik Shiksha Kosh (PSK) in Elementary Education

A two percent Education Cess was levied on all major central taxes to help finance the government's commitment to basic education. The proceeds of this Education

Cess is earmarked for the non-lapsable fund called *Prarambhik Shiksha Kosh* (PSK) and would be spent exclusively on SSA and Mid-Day Meal Scheme (Box 1).

Box 1: Prarambhik Shiksha Kosh (PSK)

- ❖ A two percent Education Cess was levied on all major central taxes through the Finance (No.2) Act, 2004, to help finance the Government's commitment to "quality basic education". Education Cess is being increased to 3 percent since 2007-08 to cover secondary and higher education too.
- ❖ In order to receive the proceeds of this Education Cess, this Ministry has created a dedicated, non-lapsable fund called *Prarambhik Shiksha Kosh* (PSK) that would be spent exclusively on SSA and Mid-Day-Meal (MDM) Scheme.
- ❖ A provision of Rs 8,746 crores for the initial transfer to the newly created PSK has been made in the Union Budget 2006-07 against estimated receipts of Education Cess. During the year 2006-07, the Schemes of SSA and MDM will be financed from PSK to the following extent:-

Source: *Annual Report, 2006-07, MHRD, Government of India. (Box No. 1)*

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

1) How many types of resources mobilisation we have?

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2) What is graduate tax?

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3) What is education cess?

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● **Non-governmental Resources Mobilisation**

State funding alone may not be adequate to meet the daunting task. The fast expanding enrolment at all stages of education has necessitated harnessing of non governmental

resources for educational development. This is more so because there has been substantial decline in the contribution from private sources under charity provision of education.

Major systematic attempts to raise non-governmental finances need to be confined to higher education. But in case of school education, the role of the community is believed to be potentially significant. At the same time there appears to be no case for fees, nor for increased role of the private sector in basic education. Hence, different criteria of resource mobilisation are to be adopted at different levels of education.

9.4.4 Community Resource Mobilisation

Conventionally, at the local level, resources are generated by the schools/education authorities from the community in a variety of ways. In some areas, villages contribute in cash and/or kind towards the construction of school buildings, in the form of monetary donations, free labour, etc. Small donations and gifts in cash and kind towards educational development is also common in many villages. Further, schools also generate their own resources through small production activities, such as production of vegetables and flowers in the school garden, production of saleable material from school related crafts and vocational classes in the schools. While it is important to encourage schools to generate such resources, caution should be taken that these measures do not put unnecessary burden on school teachers and principals. In other words, these activities should not lead to disturbance in core educational activities. Secondly, such measures are better left to the school authorities to be implemented on a voluntary basis rather than making it compulsory.

The beginning of 1990s, community resource mobilisation has been viewed as one of the favoured sources of income for the Governments in elementary education. The Education Guarantee Scheme is an important endeavour in this direction. Government of Madhya Pradesh initiated alternate schools under the Education Guarantee Scheme (EGS) in 1997. Habitations not having a primary school within one kilometer radius, with 40 children (25 to 30 in tribal areas) will be entitled to have an EGS type school. The poor local community needs to identify teachers (*Guruji*) who would be then trained by the Education Department. The scheme presumes that a full formal school with all the required basic facilities is not necessary, and hence qualified trained teachers are dispensable. The community to provide land/ space for schools, manage mid-day meal through the Panchayat and participate through Village Education Committees and Parents Teacher Association. The premise of EGS is that a community must demand a school facility, rather than receive as an entitlement / a right from the government, implies shifting the responsibility of opening schools from the government to those of people and community themselves. In 1999-2000, it became the national strategy to provide universal physical access to children living in small habitation.

9.4.5 Fees

At the school level, the issue of mobilisation of resources through fees is of a very limited nature. *At the primary and upper primary levels, since education is to be provided free, the tuition fee has no role at all in mobilizing resources for education.* However, in some states, aided private schools are allowed to charge the tuition fee, and many schools charge fees other than the tuition fee. In higher secondary schools, the tuition and other fees are paid by students. On the whole, fee-financing of education at the school level is very limited.

But in the fast changing scenario of higher education, if universities are to keep pace with development, they have to enlarge their resources base and make efforts to enlarge their internal resources by mobilizing participation of society in higher education. A commonly suggested revenue generating method in higher education is to increase fee rates. **There are two basic categories of charging fees one on the basis of cost of education is a mere economic principle and another on the basis of equity and economic principles that of universal fee or discriminatory fee.** On the basis of economic principle, four major ways in which fees (or price of education) can be charged. They are:

- **Token Fee:** It can be a nominal fee which can be uniform fees or varying across different courses and also across graduate and postgraduate levels. This can be less than 5 per cent of the total cost of higher education. The purpose here is not to mobilize resources from students.
- **Minimal Fee:** Unlike the token fee, the minimal fee is a method of mobilizing some additional resources from students. It can be either uniform fees or varying across different courses and also across graduate and postgraduate levels. The total fee income in this case will be around 20 to 25 per cent of the total cost of higher education.
- **Full Cost fee:** In this case, it is a full cost recovery, the actual cost of education is recovered from students in the form of fees. Here also, it can be a uniform fee or a varying fee (with some cross subsidization).
- **Above Full Cost Fee:** In this case, the fees charged are higher than the actual cost of education. Many of the private higher education institution charge such fees. For example, the self financing unaided private educational institutions are coming under this fee category.

The **advantages** of a discriminatory fee structure implies that fee will be charged according to the paying capacity of the student, the fee to be levied based on the cost of providing education for each faculty or subjects on the one hand and paying capacity of individual students on the other. Needless to add, those belonging to the highest socio-economic households will pay the most, close to the full pricing of education. Students from the lowest social and economic households will pay the least which indirectly helps target subsidies in favour of the poor. One can argue that discriminatory pricing may lead to an increased income for higher education without adversely affecting equity considerations in educational provisions.

9.4.6 Principles of Resource Mobilisation through Cost Recovery

Three basic principles need to be considered in mobilising resources for education:

- Resources should be adequated to provide good quality education to the target group of population.
- Mobilisation of resources should not affect the quantity of education, i.e. it should not lead to reduction in overall enrollments.
- Mobilisation of resources should not adversely affect equity in education, i.e. the demand for education of the weaker sections should not come down.

There are certain basic principles, could be noted as guidelines while increasing fees or recovering the costs of higher education from students.

- (i) **Adequacy of resources** is the most important criterion that should guide educational planners in mobilizing resources for education. Otherwise, with an insufficient level of resources, both the quality and quantity of educational activities is affected.
- (ii) While attempting at the mobilisation of additional resources from any source, it is necessary to look at the **elasticity of demand**, i.e. likely change in enrolments for a unit change in the collection of resources (fees). For example, if students are charged an increase in fee by Rs. 100/- per student, what is the likely change in the demand for such education (in enrolment)? Elasticity of demand, for a change in fees, is estimated as follows:

$$\text{Elasticity} = \frac{\text{Per cent Change in enrolment}}{\text{Per cent Change in fees}}$$

If the coefficient of elasticity is equal to one, it means that 1 per cent change (increase) in fees will result in 1 per cent change (decline) in enrolments. If it is less than one, it is called 'less elastic', i.e. a 1 per cent change in fees will result in less than 1 per cent change in enrolments. If the value of the coefficient is more than one, it means that 1 per cent increase in fees will result in more than 1 per cent (more than proportionate) fall in enrolments.

The same ratio can be estimated conversely also to find out the **revenue elasticity** to change in enrolment. This can be estimated as follows:

$$\text{Elasticity} = \frac{\text{Per cent Change in fees}}{\text{Per cent Change in enrolment}}$$

Such a coefficient helps in estimating how much revenue could be generated with increase in enrolments. Given the objective of educational planners, particularly in school education, i.e. increase in enrolments, it is important to see that the introduction of increase in fees, and other methods of mobilisation of resources will not result in fall in enrolments.

- (iii) The third principle that should be considered while attempting the mobilisation of additional resources is ensuring **equity in education**. Equity can be measured in a variety of ways. Here we consider, for simplicity, enrolments belonging to weaker sections as a proportion of total enrolments. It is possible that a particular method of mobilisation of additional resources, say increase in tuition fee in secondary schools, will not result in fall in overall enrolments. But it might reduce the enrolments of weaker sections, say girls or children belonging to socially deprived sections.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

- 4) How non-governmental resources can be mobilised ?

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- 5) Mentioned four major ways of fee on the basis of economic principles can be charged?

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- 6) Mention the three basic principles in changing the fees from students.

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9.4.7 Other Sources

Let us discuss some other resources that contribute to the development of higher education:-

Higher education institutions may mobilize resources within the institutional level such as income generating enterprises / activities, own income generation of the institutions through Guest-house lettings, printing services, conference lettings, sports facilities, sale of services/output, etc.

On similar lines, external resources can be mobilized through participation/ contribution/ consultancy from individual Indians or non-resident Indians, Alumni Associations, public and family trusts, industrial/ business houses, cooperatives, professional associations, unions/association of employees, municipalities/panchayats, MP/MLA/ Counsellors' funds, MoU (Memorandum of Understanding) with foreign universities, consultancy, endowments / donations, instituting chairs, community contributions, corporate sector donations, financial support from industrial and commercial firms – in the form of grants or scholarships for specific academic or professional programmes and inclusive children, NGOs etc.

The new partnership of education with industry and various income and profit generating sectors will have to be developed to meet the resource constraint. Stress has also to be laid on cost-effective designs of structures and methodologies of education that can cater to the needs of the massive programmes of education. The advances in information and communication technology, especially satellite-based teleconferencing, have made it possible to use distance education for training in virtual classrooms (e-learning). It is expected that technology, with appropriately designed software and quality inputs will at the same time bring down the costs and increase the efficiency of the educational system.

9.4.8 New Approaches

New and unconventional approaches for resource mobilisation should be adopted. Such illustrative approaches are:

- Examining and emulating states in collecting resources from employers, industries/ local bodies, and big industrial enterprises.
- Every higher education institution to have a College / University Corpus fund

which could be operated by school or departmental head for standard purposes like repairs up to a limit.

- Employees and industrialists using the products of higher technical institutions should be called upon to bear part of the cost of such education.
- Employees should be encouraged to set up a fund which will enable any employee to pursue any course of education which will be financed out of this fund in the course of his/her working life, tax rebates could be given for this purpose.
- Every industry should set apart out of its profits a fund for taking care of obsolescence in technology.
- In line with Industrial Finance Corporation, and such other banking and financial institutions, educational financial corporation should be also established.
- Bank may be called upon to invest in education with long term recovery schemes as is prevalent in agricultural and industrial loans.
- The sharing of academic and infrastructural resources .
- The Central Government may start duration linked Education Bonds with a view to mopping up additional resources.
- A National Education Fund of Rs. 1000 crore should be created.
- Public Sector enterprises should allocate a percentage of their budget for production and manpower development.
- A part of the cost of education should be realized from the professional institutions employing the products of educational institutions.
- Private entrepreneurs may be encouraged to contribute for educational development, particularly in respect of vocational and professional streams, by giving suitable tax rebates on their donations and by setting up of training institutions in collaboration with them. It should be made obligatory of the industries to provide for the education of their employees and the children.

Greater attention should be paid to the management of financial resources so that these are used in the most optimum manner. Relationship between inputs and outputs (efficiency indicators such as cost per graduate – the normal unit cost and the cost per successful student or effective unit cost) needs to be examined in regular intervals. There need to be generation of useful financial indicators such as modern financial management systems – routine production of financial effectiveness and efficiency indicators.

9.5 EXTERNAL RESOURCES FOR EDUCATION

External resources for education are mobilized through several international agencies. They are either **bilateral** or **multi-lateral**. The bi-lateral organization include only two countries only - the donor country(ies) and the receiving country. The examples of bi lateral organization include Swedish International Development Corporation (SIDA), Development for International Development (DIFD), etc. while multi lateral organizations include United Nations Children's Emergency Fund (UNICEF), United Nations Educational, Scientific and Cultural Organisation (UNESCO), World Bank, etc. Both **bilateral** and **multilateral** organizations provide aid in forms of grant and loans. Grants are purely aid and need not be repaid. But loans are to be repaid.

Again loans can be of either hard or soft loans. *The hard loans are called hard loans because they are given to the hard sector like steel, power in addition to harder terms and conditions such as with higher rates, shorter maturities and with no grace periods. On the contrary, Soft loans are obviously for soft sector like health, education, rural development, etc with low (or no) interest rates, long maturities and with grace periods. Soft loans are offered for 50 years with no interest, only a service charge of 3/4 of 1 percent.*

Since the mid 1980s, when the attention of the international agencies shifted in favour of poverty alleviation, the role of primary education in poverty alleviation was recognized. The share of primary education has become significant in total education lending. A clear shift in favor of primary education can be noted after the **Jomtien Conference on Education for All**. Generally the external resources that flow into the education systems are expected to be additive to the domestic resources, and that they would not substitute the national efforts. But it is not necessarily the case always.

External assistance can play an important catalytic role in the development of education, but relative to the countries' domestic education budgets, the external assistance for education is generally very small. Externally aided projects should become sustainable over time. Countries with low levels of income and educational development need to be provided assistance in terms of technical assistance as well as physical (material and direct monetary) inputs. Countries with low levels of income and reasonably high levels of educational development do not require technical assistance; external aid may be concentrated on direct money inputs, and material support. Countries with high levels of income and low levels of educational development need to be provided external aid in terms of technical assistance. Countries with high levels of income and educational development obviously do not require any kind of external assistance for education. The efforts of donor agencies in all categories of countries should concentrate on building national capacities and long term development of education in the country concerned.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answers with those given at the end of this unit.

7) What are the external resources for education?

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8) Mention any two new approaches for resources mobilisation could be adopted in any area for education.

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A number of measures as policy options have been suggested for mobilizing resources for education, which may be classified as short-term and cost control measures; and, cost-effective and long-term measures. It is often suggested that the prospects for cost reduction and increasing intensity of resource use through measures such as raising student-teacher ratios and class size, encouraging double or multiple shifts in an educational institutions, use of distance mode, school mapping, alternative modes of delivery; declining average teacher costs through recruiting para teachers and declining the unit costs by restructuring curriculum, limiting non-salary costs, training teachers to teach several subjects and reducing the length of secondary schooling. All these measures would come under the first category - cost-control and short-term measures, which will seriously affect the growth, balance and quality of not only the secondary education system but also the entire education system (Table 9.1).

Other set of policy options, which are cost-effective in nature consist of - increasing teacher utilization; reducing repetition and drop-out rates; ensuring effective school management and increasing school size to an optimum level. All these measures are cost-effective measures and will certainly improve not only the resource availability but also the quality, balance and growth of the education system. Education systems with such improvements are the bonanza to the system as a whole. But, it would require very strong governance and management.

Table 9.1 Various Policy Options on Mobilisation of Resources in Education: Its Nature and Impact

Policy Options	Nature of the Option	Impact / Remarks
Enhance overall allocations to the education sector	Long-term	Total resources available to the education sector will augment
Shift resources from other levels of education	Short-term	Secondary education development at the cost of other levels of education.
Decentralised financing		Local governments should have the power and revenue raising potential
Reduce the length of secondary schooling	Short term and cost - control measure	Quality is at risk
Decline the unit costs by restructuring curriculum		
Increasing PTR and class size	Cost - control measure	Quality of the education system will be at stake
Declining average teacher costs – para teachers	Cost-control measure	Quality is at risk
Limiting non-salary costs	Cost-control measure	Share of non-salary costs is already less in developing countries. But important item like student welfare is already less and will be nil
Increasing school size	Cost-effective measure -	given that the school operates under the economies of scale (declining unit cost and marginal costs)
Reducing repetition and drop-out rates	Cost effective measure	Quality will also improve

Reducing capital costs	Cost-control measure	Share of capital costs is already less in developing countries. This will adversely affect the growth of the system.
Alternatives modes of delivery	Cost – control measure	Quality is at risk; creating inequities in the system
Cost recovery and community contributions -Tuition fee -Learning material fee -Subsidised loan scheme -Food and boarding fee	Equity at stake unless poor students are fully financially supported	Students from low-income families are affected.
External assistance	Short-term	Can only lend a helping hand but can not sustain

* PTR : Pupil Teacher Ratio.

Besides these cost-control and cost-effective measures, a number of policy options are often suggested which seriously affects either quality and growth or equity and balance of the system. Shifting resources from one to other levels of education or reallocation of resources within the education sector is often opted for which is tantamount to saying that growth of secondary education at the cost of other levels of education. Interdependence between different levels of education is often ignored. It is essential to note that primary education forms an organic link to secondary and then secondary education forms a synergetic link to senior secondary and higher levels of education.

Check Your Progress

Note : a) Space is given below for writing your answers.

b) Check your answer with those given at the end of this unit.

- 9) Discuss the use of alternative modes of education in the context of nature and impact in secondary education.

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9.7 LET US SUM UP

We have described the various ways of mobilizing resources for education and observed that the government is the most important source. Since most institutions are financed by the government, mobilisation of resources from non-governmental sources for education has not been a major task till 1990s. Since 1990s, the extent of mobilizing resources from students in the form of fees, and a few contributions in cash and kind from the rest of the community, including parent-teacher associations, etc have been on the rise. However, given the world experience and desirability, the education system cannot depend upon non-governmental sources to any significant extent. Governments-Central, state and local layers of administration have to provide adequate resources for education, mobilizing resources through general and special

taxes and other efficient methods. Non-governmental resources could be seen mainly as supplementary resources for the supplementary activities.

9.8 UNIT END ACTIVITIES

Organize a discussion forum with your peer-students in your study centre and discuss Various ways on the resource mobilisation in education sector in your state /district. Write a report.

9.9 REFERENCES

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9.10 MODEL ANSWER TO CHECK YOUR PROGRESS

1. Internal and External resources.
2. The graduate tax in education specify tax levied on those who use educated manpower. It is a tax on every graduate who is employed in an organisation.
3. The term cess generally means a tax. Educational cess is the cess or tax collected specially for deployment in education.
4. Ref. section 9.4
5.
 - a. Token fee
 - b. Minimal fee
 - c. Full cost fee
 - d. above full cost fee
6. Ref. section 9.4.6
7. External resources for education are mobilised through several international agencies. They are either bilateral or multi-lateral. The bi-lateral organization include only two countries- the donor and receiving countries. Example- SIDA, DIFD. And Multilateral organizations include UNICEF, UNESCO, WORLD BANK, etc. Grants are purely aid and need not be repaid.
8. Ref. subsection 9.4.8
9. Ref. section 9.6

MES-044 Institutional Management

Block-1 Management of Curriculum

- Unit-1 Classroom Management (Instructional Management)
- Unit-2 Curriculum Transaction
- Unit-3 Management of Evaluation
- Unit-4 Management of Academic Resources
- Unit-5 Management of Curricular & Co-curricular Programmes & Activities

Block-2 Management of Financial Resources

- Unit-6 Educational Finance: Meaning, Importance and Scope
- Unit-7 Cost and Budgeting
- Unit-8 Accounting and Auditing
- Unit-9 Resource Mobilization

Block- 3 Management of Human and Administrative Resources

- Unit-10 Management of Student Support System
- Unit-11 Management of Administrative Resources
- Unit-12 Management of Human Resources

Block-4 Management of Infrastructure

- Unit-13 Concept, Importance, Need
- Unit-14 Management of Physical Resources
- Unit-15 Utilization of Infra-structural Resources

Block-5 Total Quality Management

- Unit-16 Quality Control, Quality Assurance and Indicators
 - Unit-17 Tools of Management
 - Unit-18 Strategies for Quality Improvement
 - Unit-19 Role of different Agencies
 - Unit-20 Quality Concerns and Issues for Research
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SOE/IGNOU/P.O. 2T/Nov. 2009



ISBN-978-81-266-4268-7