CHAPTER TWO

FINANCIAL MANAGEMENT

OF UNIVERSITY
Pivotal Role of Financial Management in Modern Universities:

Financial Crisis-Result of Management Crisis

Strength or weakness of any system is revealed when it faces external difficulties and internal pressures. The same applies to the financial management system of a university. If the system is good and efficient, internal pressures will be minimum, as they would not be allowed to accumulate and it will develop fresh means to meet the external difficulties successfully. But as it was not so and as the universities continued with the traditional system of financial management, many of them plunged themselves into financial crisis and the future did not look bright when the external unfavourable circumstances surrounded them and internal pressures accumulated.

Change in the External Environment.

There was inflation and as a result, prices of goods, materials, equipments and services increased and the salaries of the staff also had to be enhanced. Rates of interest also soared. Thus cost of Education was on a rising trend. But there was resistance to the increase in tuition fees. People were not ready to pay higher taxes and higher tuition fees for their wards to meet higher costs faced by the universities. This was because inflation had also reduced the real incomes of the common people and hence had decreased their capacity to pay more taxes or more fees.

Another external phenomenon that had developed was growing unemployment of the educated persons which showed lack of coordination between the requirements of the labour market and the university products. It was thought that primary and secondary education deserved a greater allocation of public resources and the benefits of higher education were found to be less than their costs. This belief was not completely justified
and there was only partial truth in it in the sense that there was no linkage between the requirements of the growing labour market and courses and subjects taught in the universities. There was mere drifting with the currents of the winds.

On the other hand, there was now greater insistence by the government and the people for accountability on the part of the universities. People wanted to know whether taxes or fees that they paid were efficiently utilized by the universities or not and whether in the right directions. Faith in universities had eroded itself.

In response to changes in the external environment for higher educational institutions, change in the functions of financial management should take place. The main changes in the external environment were on the following lines:

(1) Many governments in the world have evolved programmes of financial austerity for higher education institutions.
(2) There has been continuous expansion of student enrollments.
(3) Accountability of educational institutions, particularly of universities, is insisted upon by the society and by the government.
(4) There is a drive towards more autonomy and devolution of responsibility from the state to the universities and within the university, from the centre to the constituent units.

So, in the context of the financial crisis and change in the environment and pressure for accountability, universities should endeavour to introduce some basic changes in the management of their finance.

About the external environment influencing the universities in the present times, I would like to quote John Pratt and Geoffrey Lockwood. They write: the fundamental purposes of universities of creating and
transmitting knowledge through teaching and research require a substantial degree of institutional independence. The mechanism of the UGC is itself an attempt to secure freedom from undue interference by government; the basic elements of the system for academic staff appointments protects their freedom to pursue and publish their personal studies and teach free of political pressures. But the functions of universities make them subject to legitimate public interest in their affairs and how they conduct them. They consume public funds and employ human and other resources; they produce educated manpower; they are ultimately servants of society in their production of knowledge, however abstruse. Throughout their histories, the universities have had to strike and maintain in their constitutional arrangements and their day-to-day management a balance between the two demands for independence on the one hand and of public accountability on the other. In particular, it is a key task of university managers to relate their internal structures, processes, practices and plans to the demands of both the academic community and the world outside the campus. This task is taking on new and increasingly challenging dimension in the closing decades of the twentieth century.

"These external pressures and exhortations are numerous. Universities need: to economize; to adapt to the needs of current society; to train the teachers; to make their teaching and research more relevant to the requirements of the economy; to improve the standard of behaviour of the members; to be more democratic in their government; to serve the local community; to concentrate upon the development of science and technology; to maintain an awareness of their role as the protectors of the national cultural heritage; to encourage creativity; to have a closer relationship with industry; to educate people to live in the world of the
twenty-first century; to take their responsibilities to the international worlds of trade and learning more seriously; and be more positive in providing opportunities for the mature, the disadvantaged, etc. These and many other, often contradictory demands and assertions are frequently made about the university. They are predominantly external in origin although each finds some degree of internal advocacy.

The autonomy, pluralistic nature, and the gradualism of universities limit managerial power. The few people who form the government and management of a university at any one time are the shock absorbers in the system in between the external pressures of change and the internal institutional resistances.

"The force and direction of external pressures on the universities stem ultimately from basic national factors. Thus, the universities have to share in financial hardship arising from overall economic performance just as they once were able to benefit from national prosperity; they are victims as well as beneficiaries of demographic trends; they operate in a world of changing social, political and technological features, all of which influence their operation. The effects of the factors are complicated, since they interact and may contradict or reinforce each other. But changes in the factors may not only have direct effects on the universities, changing the resources available to them, the markets upon which they depend and their operating practices, but also create or condition the views of external bodies about the educational, social and economic functions of the universities. For the universities are subject to the influences and controls of a multitude of external bodies which in varying ways and to varying extents impose, interpret or mitigate pressures of the
external world upon them. It would not be appropriate, even if it were possible, to identify all these bodies here, but the primary sources are Parliament, Government, the Department of Education and Science, public opinion, the University Grants Committee, the Research Councils, local authorities, the Committee of Vice-Chancellors and Principals, trade unions, professions, peer groups, industry/commerce, and applicant demand". (Universities The Management Challenge)

Real Cause of Crisis is Not Without But Within

The budget crisis of Yarmouk University is also the external symptom of the same deeper internal problem of inadequate management system and a defective financial management structure. In this fast changing world when globalization is taking place and free competitive market economy is emerging at the international level, all institutions—public as well as private, have to dynamically and constructively adjust to this fast changing external environment. Response should be healthy and timely. This requires knowledge and internal vitality and mechanism to find out errors and accept them as drawbacks and activate forces to rectify these errors, instantaneously. If this basic mechanism and approach are not present, mistakes will go on multiplying with the passage of time and will ultimately take the shape of varied crises—financial and other ones. Private enterprises and institutions have to adjust more quickly, otherwise they are wiped out. Public enterprises and public institutions take time to adjust and there lies the greatest defect of the public enterprise and public institution system. Public universities are no exception to it and Yarmouk University suffers from the same type of ailments.
**Better Times of the Past**

But some years ago, there were better times—there was no inflation, no recession in the economy and so tax revenue was buoyant and hence share in tax revenue for the public universities was substantial, the number of the public universities (among whom the share in tax-revenue was to be distributed) was limited, there were no private universities to compete with and there was not much pressure by the people and the government for accountability of the public universities. But now all these factors have changed. Costs of goods and materials are now 2.5 times of what they were in 1986. So costs for the universities have gone up, but the tuition fees for the bachelor students have not been increased since 1986. Due to inflation, the tuition fees are on a decreasing scale in real terms. Share from the tax revenue is dwindling. Expenditure for salary payments has been increasing and there has taken place heavy and undue expansion of the non-academic staff in the central offices of the University.

**Suicidal Policy of Subsidy**

Yarmouk University had continued with the policy of providing food, hostel accommodation and primary and secondary school facilities at subsidized rates which were much below costs.

**Better Financial Management System Would have Averted Crisis:**

But if there would have been installed a modern scientific and sound financial management system like planning, programming and Budgeting system (PPBS), the higher management would have known the correct expenditure and revenue position earlier and would not have allowed the non-academic central staff to proliferate to such an extent as at present and would have also abandoned the policy of charging goods and services at
lower prices than their costs and they would have endeavoured to open-fresh sources of revenue for the university and the university would have been spared the financial crisis from which it suffers now.

Modern Scientific Age and the Importance of Financial Management:

Financial crisis of Yarmouk University is one of the many examples in support of our hypothesis. Many public universities in the different parts of the world suffer from the same types of financial difficulties and almost for the same reasons. In the life of an individual, family, economy, society and like-wise in the life of a university also, difficulties come in this fast changing world. Modern age is the scientific age and the system of creating technological, scientific and economic, political and social innovations have been institutionalized and hence the progress of innovations in all these fields has become very rapid and self-generating. So, the external environment is fast changing to which individuals, families, economics and specially universities have to adjust healthily and constructively. It will not be out of place here to emphasize the fact that most of these innovations are being created by the universities themselves. The process of creating innovations has been mostly institutionalized in the universities, as, along with the dissemination of existing knowledge, they are also entrusted with the task of doing research for the creation of new knowledge resulting into discoveries innovations and inventions.

So, we have to take the 'abnormal' as the normal and create internal vitality and mechanism and the system to give us correct information about our weaknesses and mistakes at right times and enable us to control the activities and rectify errors, so as to solve the problems in time before they accumulate and appear in the form of crises. For any
Institution, it is its managerial system and particularly its financial management system as the part of it, which carries great importance.

**Integral Role of Financial Management**

No institution or organisation can realize its goals and satisfy its objectives without the proper provision of finance. Finance for any organisation is like blood in human body. But as in the human body, there is not only blood, but the blood system and the mechanism to circulate it in the entire human body, in the same way, there is financial management system which occupies the pivotal position in any organisation, particularly in the public university. The notion that financial management is concerned merely with budget preparation, controlling, accounting and auditing is fast becoming out of date. It is, of course, concerned with all these activities, but its angle is different and the financial Manager as the head of the financial management system, has to be associated with the processes of planning and programming with the higher Management from the beginning. Thus the financial management system has to be an integral part of the higher management system. Before budget preparation there should be planning of the goals and their transformation into specific objectives and then programming of activities should follow to translate these goals and objectives into concrete action. This is the function of higher management, but this is hardly properly followed by higher management and where it is done so, the budget cannot be prepared in an isolated way. Budget is a means to realize the goals and objectives of the university. Budget gives a detailed work plan for different activities to be completed within a specific period of time and with allotted amount of money but unless there is programming of activities by higher management a detailed work plan of specific activities cannot be prepared. Also Unless
financial manager is associated from the beginning with planning and programming to be done by higher management, budgeting and budget preparation and detailed work plan cannot be done full justice and made a true means for the realization of the goals and objectives of the university

**Meaning Of Sound Financial Management System**

Importance of financial management is not properly realized because there is no proper idea or visualization of the vital constituents of the modern scientific financial management system. As for example take the case of an efficient information system as the part and parcel of the sound financial management system.

It should be realized that there is difference between data and information. Data consist of facts but they do not speak. Raw data does not provide meaningful information to help the policy makers to take right decisions. Unless there is analysis of data and its interpretation in the form of some financial indicators and performance indicators, data does not become meaningful so as to help the top management to take the right policy decisions and that also at right times. That is why an efficient information system is required as an essential ingredient of the sound financial management system.

It should be also realized that the different departments and faculties will have their own sub-goals and instructional programmes carrying financial implications and they all will have to be integrated as the viable parts of the integrated whole by financial management in consultation with higher management.

Actually, financial management provides a link between core financial processes of budgeting, financing, controlling, accounting, auditing, reporting and purchasing on one hand and substantive
management processes of planning, programming and evaluating on the other. Thus financial management plays an integrative role which becomes more clear with the help of the following figure given by Jerome B. Mckinney in his book “Effective Financial Management in public and non-profit Agencies”.

**Figure 2.1**

**Financial Management’s Integrative Role**

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**Integrated Financial Management**

**Defining Its Components**

1. Planning defines the goals, objectives, and priorities to be pursued
2. Programming selects the best available activities to achieve stated goals and priorities usually within a specific time period
3. Budgeting develops a specific detailed work plan to achieve stated goals and priorities usually within a specific time period.
4. Financing provides the necessary financial resources to carry out the planned and programmed objectives.
5. Controlling assures that the activities planned and programmed are carried out according to the detailed pre-established work plan.
6. Evaluating assesses the utility, appropriateness and congruence between stated goals and objectives and achieved results.
In the figure, the arrows surrounding the box of the financial management system show the integrative role that financial management plays in linking the core management processes and financial processes. The coordination of two processes can be seen as "a set of sequential steps: planning, programming, budgeting, financing, controlling and evaluating". On the higher management side, articulation of goals and formulation of objectives by them is called planning determination of appropriate activities for the realization of goals and objectives of the university as articulated through planning by core management is programming. This is the process pursued by higher management and shown on the right side of the figure in a box.

On the left side of the figure, in a box ingredients of core financial processes are given after programming by higher management. Budget is prepared by financial management which allocates the resources for carrying out the programmed activities in accordance with their priorities. After budgeting, financing of these programmed activities follows in accordance with the detailed work plan as formulated in the budget. These activities have to be carried out within allocated resources and stipulated times as prefixed in detailed work plan of the budget. So the financial management has created the control system which sees to it that there are no big variances between the estimated figures and the actual ones and if there are any, they are to be corrected and brought within tolerable limits. This is Controlling by financial management, it is not evaluation.

Then evaluation of results is undertaken by higher management which compares the ultimate results with their articulated goals and objectives for a university, these goals and objectives are the progress of the students and useful research which benefits the society and satisfies the growing needs of skilled labour and required man power and the
percentage of the students getting degrees in their respective fields, we may say that controlling follows the work-plan of the budget, while evaluation follows the goals and objectives of the university as articulated by higher management.

Need For Sound Financial Management System For Public University.

In fact, financial management is a means to promote and realize the goals and objectives of the university. It is true that it is teachers and the students who are the university and who cooperatively seek knowledge, create knowledge and disseminate knowledge and serve the society and thereby become instrumental in the development of the society and the progress and happiness of its members. But can any activity be done without the help of money?

Finance is the life-blood of every organisation and it is particularly so of the public university which does not seek profit though it uses the financial resources a great deal; profit is a surplus which can be further used for investment and growth of assets but this is not available to a public university. So wiser and efficient use of available financial resources becomes very important for the university. Seeking of knowledge and dissemination of it by the teacher and the students will suffer a setback if the finances of the university are in the doldrums. Teachers and students should be allowed to pursue their goals unperturbed. This requires a sound financial management system for a university.

Three Purposes Followed by Financial Management in a university:
(1) To maintain and if possible to enhance the ability of the university to realize its goals and objectives and to fulfil its mission,
To provide adequate financial resources to the university so that it can continue to pursue its higher goals undisturbed and without any sense of financial insecurity.

To preserve accountability of the university in the eyes of the donors, creditors, society and the government.

If we study the first purpose, we find that the financial management should try to enhance the capacity of the university to generate more revenue and reduce expenditure.

The success or failure of it may be judged by looking at the assets and the liabilities of the university. If the assets have remained stable or grown and the liabilities also either have remaind stable or have been reduced, then financial management has succeeded in its first purpose. Firstly it requires balanced budget deficits which cat away into the very vitals of the finances of the university secondly endowments should be so managed that their principal amount’s real value is at least maintained. Maintenance and modernisation of equipment should be undertaken and funds should be put aside for replacement in future also. Higher quality teaching and research staff should be maintained, retained and developed, as they are the most valuable assets for the university.

When we study the second purpose, we realize that search for revenue requires the winning of confidence of the government and the donors. It also requires efficient cash management so that good interest income can be earned for the intervening short periods and selling of services and food and other items at atleast cost prices and not below it. So that there are no subsidies. Due to deficits in a public university, tuition fees can at least be increased to some proportion of the degree of inflation. Student teacher ratio can be increased and the ratio of non teaching staff to
teaching staff may be reduced. This will increase revenue and reduce expenditure. Consultancy and research projects on the contract basis with private companies and government enterprises can be undertaken by the academic staff of the university and financial management can help the academic staff by creating liaison and providing guidelines and contacts with the interested outsiders.

It is the essential characteristic of sound management that it is always in search of ways for decreasing costs and increasing revenues without making any compromise with the quality of Education. Whatever financial management does, it is ultimately for improvement of the quality of Education.

The third purpose pertaining to maintaining accountability implies that resources should be efficiently utilized for the maximization of goal-realization so that the financiers of the university like the government, donors, parents of the students, creditors etc. can feel convinced that their money is most properly utilized. The reporting of these facts should be done in a simple and lucid way so that the sufficient flow of money from these financiers may continue uninterruptedly to the university.

**A penny Saved - A Penny Gained Principle:**

Universities in almost all the parts of the world have been suffering from severe resource-crunch and in such circumstances of financial stringency, proper and efficient management of resources becomes more important. In English language, there is a proverb that a penny saved is 'a penny gained', which means that when financial resources are efficiently used, better work is done with the same given resources. Just as in underdeveloped countries, organization is an alternative to capital, in the same
way, in a situation of resource crunch, saving of resources by avoiding of waste and their more efficient utilization is like earning of fresh revenue. Hence, in these circumstances, crucial importance of financial management for a university should become obvious and it should be accepted by all and sundry that it should be given a pivotal place in the management structure of the university.

There is another point which highlights the important role that financial management is expected to play. We know that the function of the university is to create knowledge in the process of discovery of truth and transmission of that knowledge through teaching. Seeking of correct knowledge requires perfect devotion to truth which can be utilized for human welfare. This necessitates autonomy for the university and a substantial degree of institutional independence. Institutional independence demands steady and if not completely steady, at least reliable sources of finance. Here, financial management of universities assumes great significance.

**Quality of Education and Sound Financial Management System:**

Financial management is important, because in economising resources and in finding out new sources, it is expected that the quality of education will not be allowed to suffer. Quality of education has to be maintained, otherwise financial management will not have any value. Financial management is a means to serve the goals and the objectives of the university and the efficiency of financial management lies in seeing that these goals and objectives do not suffer due to paucity of resources and they are served even better. So financial management has got a central role to play in the efficient functioning of the university.
Mr. M. L. Sobti has the following observations to make regarding this highly significant role of financial management in the university: “The university’s business is not about making profits. Nevertheless, in its management, the objective of making the most of its resources remains paramount. All time education is a stretching process, a process of reaching the limits and of going beyond, and the culture of a university’s management has essentially to foster this process. This calls above all for systems and arrangements by which the faculty and the students, the main resources of a university, are able to develop their fullest potential and contribute to the university’s goals in the areas of generation and transmission of knowledge, through research, training and extension. Finance has to serve as a major instrument in promoting such systems”.

Central Feature of Financial Management

But we have to understand the central feature of financial management in order to comprehend its decisive role. Mr. Madan Mohan Sharma has made illuminating remarks about this interesting point in his book “Financial Management of Universities in India” in the following words: “The central feature of financial management is the formulation of organisation strategies to determine the most effective use of available funds at the disposal of the organisation and the exploration of the most favourable sources of additional funds which the organisation will need in the foreseeable future. The central issue of financial policy therefore, is the proper use of funds. This process involves rational matching of advantages of potential use against the cost of alternative potential sources, so as to achieve the broad financial goals which an enterprise sets before itself. The art lies in using these funds as profitably as possible; planning future operations, controlling current performances and future development
through financial accounting, cost accounting, budgeting, statistics and other means. Financial Management is a sub-function of total management and its task is to assist in (i) allocation of resources, (ii) utilization of resources and (iii) evaluation of results". 