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Working Capital Finance for Private Unaided Educational Institutions

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Abstract:
Private Unaided Educational Institutions are expected to play a major role in the Indian Higher Education system. However, a recurring problem faced by a number of such institutions is delays in payment of salaries. One reason that is put forward by the Institutions is that the scholarship reimbursement towards fees of category students from the Government Department of Social Welfare is delayed. While this might be true, there are a couple of banking solutions that can tackle this issue. One, quite standard mechanism is the provision of a cash credit facility against the fee receivable. Another option in the form of factoring service can also tackle the problem. Based on a sample study of private unaided educational institutions in Ahmednagar District of Maharashtra, this article discusses these practical solutions.

Keywords: *Fees, higher education, scholarships, private unaided colleges*

1. Introduction

News reports in The Indian Express dated 27.03.2013, the Times of India dated 13.02.2015 and the Marathi daily from Pune, Sakal dated 22.03.2015, point out to the increasing gravity of the problems of delays in payment of salaries to staff of private unaided educational institutions. So far the news that used to flash in the newspapers was that of the suicide of the farmers. But the news that appeared on 22nd March, 2015 has sent shocking waves because it was the news of suicide by a teacher for want of payment of his salary. The phenomenon of delay in payment of salaries by private unaided educational institutions has been a regular one. Through a study of Financial Management Practices of Unaided Educational Institutions in Ahmednagar District of Maharashtra, this article tries to go to the root of the problem and comes out with some practical suggestions.

2. Research Study

A research study under the title "Study of Financial Management Practices adopted by Unaided Educational Institutions in Ahmednagar District (2003-2013)" was carried, wherein primary data was collected from 14 private unaided educational institutions of different streams like engineering, medical, pharmacy, MBA etc and 10 banks from 3 categories, nationalized, cooperative and private. The respondent private unaided educational institutions were asked to list 3 major problems in the area of short-term funding. 37% of the respondents stated that lack of cash credit facilities is a serious issue that acts as a road-block in short-term funding. Various aspects of the problem and suggested solutions are discussed in the paragraphs to follow.

3. Problem Explained

Since more than 25% of the fees are received from the Government by way of scholarship as a part of reimbursement of fees of category students, delay in receipt of such fees create working capital gap. The typical cash flow pattern and the working capital gap is presented in the form of a diagram -

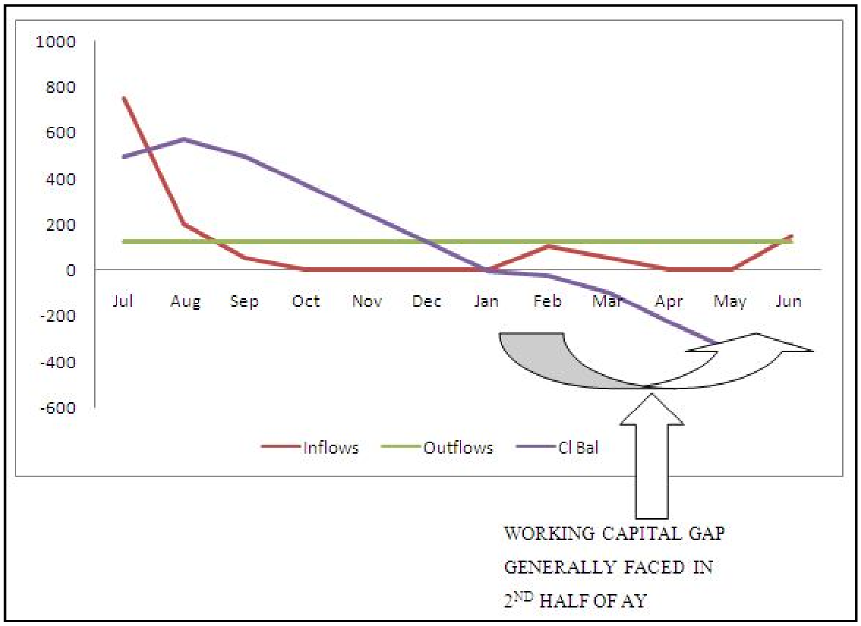

Figure 1: Typical annual cash flow pattern of a private unaided educational institution

3.1. Observations

- Cash Inflows are concentrated at the start of the academic year at the time of new admissions.
- Outflows like salaries, electricity, telephone, water etc are generally fixed costs that are required to be paid every month.
- As the institutions start approaching 2^{nd} half of the academic year (January to June), there resources dry up and the cash flows move into the deficit zone.
- This situation is particularly experienced, when the scholarships to be received from the Government for category students get delayed and a working capital gap is created.
- Educational institutions typically borrow against fixed deposit receipts or break such deposits to meet the working capital crunch. However, this amount on most of the occasions is inadequate to take care of funds requirements of more than a couple of months.

4. Suggested Solutions

The suggested solution is in the form of a cash credit facility against hypothecation of fee receivables. The facility and its operation are depicted as under

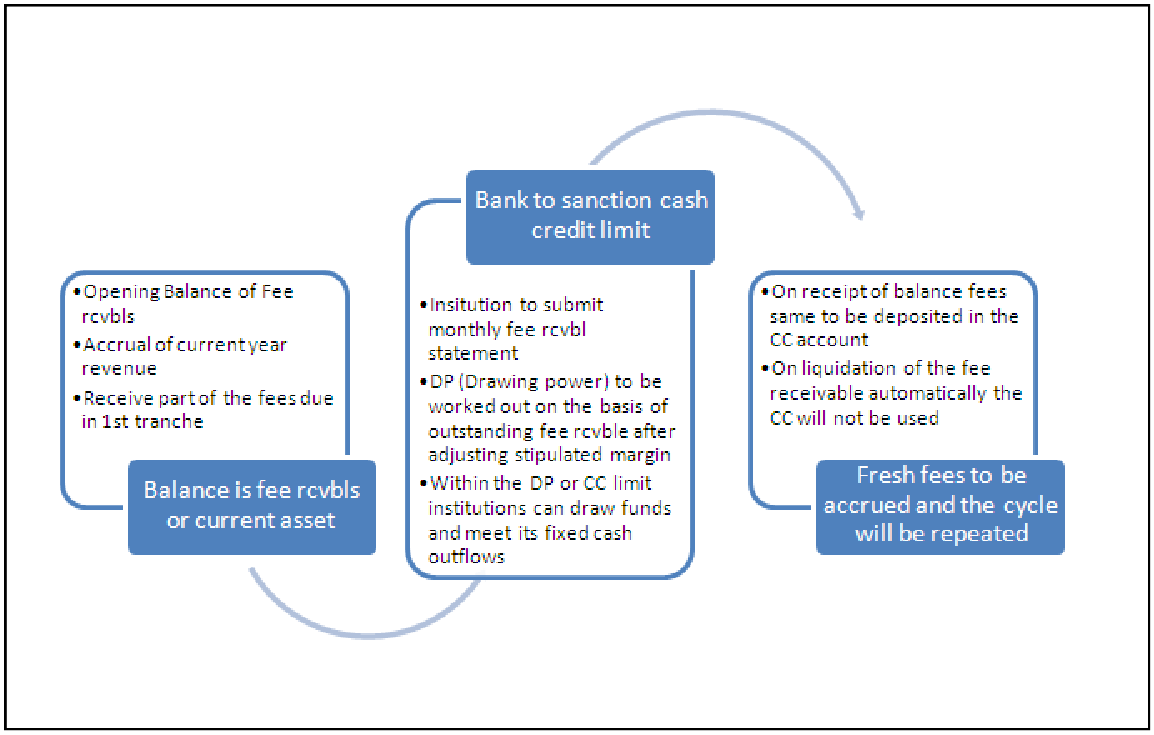

Figure 2: Snapshot of the Cash Credit model for an educational institution

5. Benefits of the CC Facility for the Institution

1. The CC facility provides the essential short-term liquidity that is so critical to avoid working capital deficiency leading to non-payment of salaries and other committed expenses
2. Since the facility is linked with outstanding fees and its receipts, the interest is charged only on the utilized limit and not on the entire sanctioned limit. As and when funds are available those can be deposited in the CC account as a result of which the interest would not be charged
3. Fee receivable can be hypothecated as a primary security. Additional collateral security may be needed but in presence of fee receivable as the primary security, quantum of collateral security is significantly reduced
4. Once the facility is sanctioned initially, annual renewal requirements are relatively simpler
5. Institutions can also enjoy benefits associated with online banking and other facilities like RTGS etc.
6. Since the institution is required to pay interest on the utilized limits of CC, it would be inclined more to manage its fee receivables in a professional manner.

6. Benefits for the Bankers

1. Since a major chunk of the fee receivables is in the form of outstanding scholarship that is to be received from the Government, risk of bad debts is minimal. Unlike private receivables, government receivables are more assured
2. Based on the monthly fee receivable position banks can lend only to the extent of DP. In other words, when the receivables are not available obviously the DP will not be there and in that case the institutions would not be able to draw the CC
3. Banks can get lot of cross-selling business in terms of accounts of employees and students
4. They can maintain reasonable checks and balances by asking the monthly fee receivable statements to be audited by Chartered Accountant. Further, it can ask its own auditors to conduct the fee receivable audit

7. Factoring Services

Specialized services like Factoring can also play an active role in not only just financing the receivables but managing the entire fee receivables management portfolio. One advantage with this arrangement can be that the educational institutions can concentrate on academics rather than an administrative task of collecting fees.

The suggested factoring mechanism in the instant case is explained with the help of following diagram –

- 1 Institution enrolls the students
- 2 Institution assigns fee receivable to factor
- 3 Factor makes prepayment up to 80%
- 4 Monthly statement of accounts to institution and follow-up
- 5 Student / Government makes payment to factor
- 6 Factor makes balance 20% payment on realization

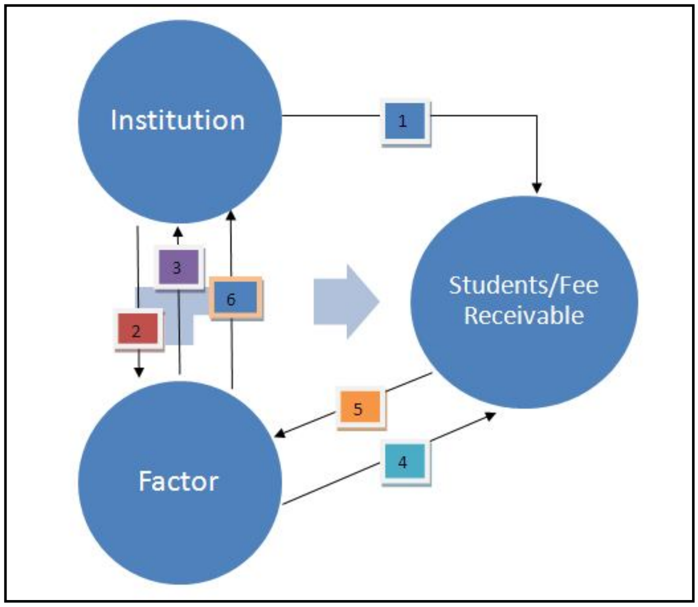

Figure 3: Modus operandi of factoring

8. Conclusion

Cash credit facility and factoring services can prove to be handy working capital finance solutions for private unaided educational institutions. The fee receivable from the Social Welfare Department of the Government is a current asset that needs to be turned into a liquid asset with the help of banks. With reservations on the rise, the amount that would be receivable from the Samaj Kalyan Department is going to increase and the problem of delays in payment of salaries by the private unaided educational institutions will only aggravate unless some practical solutions are put in place.

9. References

1. The Indian Express dated 27.03.2013
2. The Times of India dated 13.02.2015
3. Sakal dated 22.03.2015,