Meaning, definition, types and principles of budget.

Meaning of Budget:

The word ‘budget’ is derived from a French word, 'Bougette', meaning a leather bag or wallet. The term was used for the first time in 1733 in a satire entitled ‘Opened the Budget’ pointed against Walpole’s financial plan for that year. The Chancellor of the Exchequer used to carry a leather bag containing papers on the financial plans for the country to the House of Commons.

So when he set off to place his financial plans before the House, he used to open his ‘budget’, that is, the bag, and it is because of this association of the financial plan with the ‘bougette’ that the financial statement of a country has come to be known as budget.

The term budget in modern times, therefore, denotes that document which contains estimates of revenue and expenditure of a country, usually for the fixed period of one year.

Some of the definitions of the word ‘budget’ are the following:

(i) “A budget is a financial plan summarizing the financial experience of the past stating a current plan and projecting it over a specified period of time in future.” **—Dimock**

(ii) “A budget is a financial statement, prepared in advance of the opening of a fiscal year of the estimated revenues and proposed expenditures of the given organisation for the ensuring fiscal year.” **—Harlod R. Bruce**

(iii) “Budget is a plan of financing for the incoming fiscal year. This involves an itemized estimate of all revenues on the one hand and all expenditures on the other.” **—Munro**

(iv) “Budget is a detail of estimated revenues and expenditures-a comparative chart of revenues and expenditures-and over and above this it is an authority and direction of the competent authority given for the collection of revenues and expenditure of public money.” **—Wilne**

(v) “Budget is a document containing a preliminary approved Plan of Public Revenue and Expenditure.” -**Storum**

(vi) “The budget in a modern state is a forecast and an estimate of all public receipts and expenses and for certain expenses and receipts an authorization to incur them and collect them.” —**Rene Gaze**

(vii) “Budget is a financial plan of government for a definite period.” **—Taylor**

From the above definitions of budget we conclude that the following are the elements of budget:
(i) It is a statement of expected revenue and proposed expenditure;

(ii) It requires some authority to sanction it;

(iii) It is for a limited period, generally it is annual;

(iv) It also sets forth the procedure and manner in which the collection of revenue and the administration of expenditures is to be executed.

The budget is the nucleus round which the financial activities of the state oscillate. It is both the scale and the limit of all the financial operations. However, it may be noted that the meaning of budget is no longer confined to a mere statement of the estimated revenue and expenditure. It is now given a wider meaning.

With the gradual development of financial management, it has come to include not only a plan of public revenue and expenditure but also “the entire condition of material finances as disclosed in the ministerial statement placed before the legislature and the orderly administration of the financial affairs of the Government.”

It **“not only gives an account of the year’s ‘housekeeping’ and of the year to come so far as the State is concerned, but it is the basis of control of the financial affairs of the State regarded as a household. It sets in motion a continuous chain of events of great importance in the everyday work of the Government.”**

Functions

The following points highlight the functions or purposes of budget.

1. It ensures the financial and legal accountability of the executive to the legislature.
2. It ensures the accountability of subordinates to superiors in the administrative hierarchy.
3. It is an instrument of social and economic policy to serve the functions of allocation, distribution and stabilisation.
4. It facilitates the efficient execution of the functions and services of government.
5. It facilitates administrative management and coordination as it unifies the various activities of the government departments into a single plan.

Types of budget are as follows:

1. Annual or long-term budgets:

Generally, the Government budgets are annual, i.e., they are prepared for one year. In India, England and most of the other commonwealth countries the financial year begins on 1st of April and ends on the 31st of March, but in the U.S.A., Australia, Sweden and Italy the dates are 1st July and 30th June. In France these dates are 1st of January and 31st of December.

Some countries have adopted the policy of planned economy and to meet the needs of long-term planning, they have resorted to long-term budgeting, i.e., preparing the budget for three or more years. Such budgets are in fact long-term planning rather than long-term budgets because what is provided for is financial planning over a period of years to finance the plan.

These countries spread the estimated plan expenditure over a number of years. The legislature approves the plan along with its estimated expenditure, but that does not amount to actual voting of appropriations for the entire period. Every year the national budget will include the expenditure on the plan for that year which will be approved by the legislature.

2. Single or plural budget:

When the estimates of all the Government undertakings find place in one budget, it is known as single budget. The advantage of single budget is that it reveals the overall financial position of the Government, as a whole.

But if there are separate department-wise budgets which are passed separately by the legislature, it is called plural budgeting. In India we have two budgets—one for the railways and the other for all the other remaining departments. The practice of having a separate railway budget started in 1921. In England there is single budget.

3. Surplus, deficit or balanced budget:

A budget is surplus if the estimated revenues are in excess of the estimated expenditure. But if the anticipated revenues fall short of the anticipated expenditure, it is a deficit budget. According to the economists, a deficit budget is a sign of the country's making progress. A balanced budget is one wherein the anticipated revenues equal the/anticipated expenditure. The budgets are generally deficit budgets.

4. Cash or revenue budget:

A cash budget is one wherein the estimates of the various items of income and expenditure include the amounts actually to be received or spent in one year.

In revenue budget the revenue and expenditure, accruing in one financial year, are budgeted in that financial year irrespective of the fact whether the revenues are realized or the expenditure is incurred in that financial year. In India, Britain and U.S.A., there is cash budgeting, in France and other continental countries there is revenue budgeting.

5. Departmental or performance budget:

The present practice is to have departmental budgets, i.e., the revenues and expenditure of one department are grouped under it. It does not give any information as to the activity or performance for which money is budgeted. The performance budget is one where the total expenditure of a particular project is grouped under the head of the particular programme.

It is prepared in terms of functions, programmes, activities and projects, for example, in the case of Education (a function), it will be divided into programmes like those of Primary, Secondary and Higher Education. Each programme will be divided into activities, for example, training of teachers is an activity. Project is the last unit of functional classification.

It signifies such an activity as is of a capital nature, such as, construction of a school building. The A.R.C. has recommended the adoption of performance budgeting in all the departments and organizations of the Central and State Governments which were in direct charge of development programmes.

Principles of Budget-Making:

Budget is an effective instrument of economic and social changes. It is the basis without which there can be no lasting social progress. It is desirable that it should conform to certain budgetary principles.

Important principles of budget-making are the following:

1. Budget should be a balanced one:

Budget should be a balanced one, i.e., the estimated expenditure should not exceed the revenue or income. When the amounts of the expenditure and revenue in a budget are equal or nearly so, it is called a ‘Balanced Budget’. If the expenditure is less than the anticipated revenue it is a ‘Surplus Budget’ and if the expenditure is more than the anticipated revenue, it is called a ‘Deficit Budget’.

“The balancing of the Budget,” says, Mr. P.K. Wattal, “is the first requisite of financial stability, and occupies the same place in the financial administration as the maintenance of law and order in the Executive administration. On the other hand, un-balanced budgets are bound sooner or later to weaken the faith of investors and lead to monetary inflation, which if uncontrolled will terminate in national disaster.”

An occasional deficit budget, however, need not cause worry. The newer trends of economic thought consider deficit budget in certain circumstances not only excusable, but also necessary.

According to them, a deficit budget can cure the ills from which the modern capitalist economy suffers. Deficit budget has now become a common phenomenon of the developing countries. It is resorted to, to meet the huge costs of development plans. However, it is not safe to indulge in deficit budget beyond a certain point.

2. **Budget formulation is the responsibility of the executive:**

As the Chief Executive is responsible for running the administration, he is in the best position to say what funds are required for it. It should, therefore, be the duty of the Chief Executive to formulate the Budget. But the Budget framing is a stupendous task and he must, therefore, be aided and advised by a body of specialists.

In India, the Ministry of Finance, in England the Treasury and in U.S.A. the Bureau of the Budget, help their respective Chief Executives in the Budget-planning. In Parliamentary government, there exists the well accepted principle 'that no demands for grants can be made except on the recommendation of the Executive'.

The principle also makes it clear that it is the function of the Executive alone to prepare the budget. The Parliament can decrease or refuse the demands presented to it by the Executive but it cannot increase them.

This principle is of great merit because the Chief Executive being the actual expending authority is the better judge of how much money is required for a particular purpose and if more is given to the Executive than what it needs, it cannot be made responsible for money it did not need.

That would obviously lead to wastage and extravagance. This last principle is not strictly followed in the U.S.A. as there is a separation of powers and all legislative functions including those of money bills are those of the Congress which is accordingly competent to decrease as well as increase expenditure and taxation.

3. **Estimates should be on a cash basis:**

The principle of the cash basis of the Budget means that it should be prepared on the basis of actual receipts and expenditure expected during the year and not on the basis of receipts which are to be realized in some other years or the expenditure which is ordered in that year but is likely to be incurred in the next financial year, e.g., if certain sums on account of arrears of tax relating to the year 1971-72 are realized in the year 1972-73 they should be shown in the receipts estimates of the latter year and not of the former.

Similarly, if the liability for any payments was incurred in the former year but was actually met in the latter year, it should be shown in the expenditure of the latter year only.

In the words of P.K. Wattal; “One advantage of having cash estimates is that the public accounts can be closed very much earlier than when they are prepared on a demand and liability basis. In some European countries, where the latter practice is followed, the determination of the final surplus or deficit requires years and even decades. Delayed accounts lose much of their value for purposes of financial control. The French Budget for 1920 was finally closed in the beginning of 1937.”

4. Budgeting should be done on the basis of gross and not net income:

Budget should present a clear-cut picture of the gross and not the net income of the country. Both the receipts and expenditure should be fully shown in the Budget and not merely the resultant net position. For example, if there is a department with an estimated expenditure of Rs. 45 lakhs and receipts of Rs. 35 lakhs it should show in the Budget both the expenditure and receipts and not merely Rs. 10 lakhs only.

If the department prepares the estimates on the net basis, it would mean that it would approach legislature for grant of Rs. 10 lakhs only and hence deprive the legislature of its control over the expenditure of Rs. 45 lakhs, which it met out of its receipts. Gross budgeting is, therefore, essential to ensure complete financial control of the Legislature.

5. Estimating should be, as far as possible, exact:

Estimates provided in the Budget should be, as far as possible, exact. There should be neither too much of over-estimating nor under-estimating. While money should be provided for all necessary expenditure, the amount provided for should be the absolute minimum.

If there is over-estimating of expenditure people are unnecessarily heavily taxed and if there is underestimating, the whole budget may be thrown out of gear when it comes to execution.

It is a tendency on the part of the departments in India to under-estimate their income and over-estimate their expenditure although there are clear instructions to the Heads of all the Ministries, that they should try to achieve economy and avoid waste as far as possible.

Close and exact estimating can be achieved by taking past three average figures of the receipts and expenditure under various heads as the starting basis and making appropriate variations due to special circumstances which can be foreseen.

Secondly, estimates should be itemized, that is the detailed estimates should be divided into major-heads, minor- heads and sub-heads and detailed heads of revenue and expenditure.

Close budgeting also means that the services for which provision has been made and the particular items included in any vote should be specified and that no demand of ‘lump sum’ amount under any head should be granted.

Of course, in some departments, such as Public Works Department, block grants cannot be avoided because we cannot have definite assessment of the amount likely to be spent on repairs and maintenance of government buildings, canals or roads, etc.

But, subject to these exceptions, the general rule should be that no demands for lump sums for unspecified purposes should be sanctioned. Such demands escape Parliamentary control of Public expenditure and should be granted only in very exceptional cases.

6. **Annuality of the budget:**

The principle of annuality is one of the most important principles of budgetism. It means that the budget should be prepared on the annual basis. In other words, it means that the legislature should grant money to the Executive for one year.

A year is a reasonable period of time, for which the legislature can afford to give financial authority to the Executive. It is also the minimum period which is necessary to execute the financial programme. But annuality of the Budget does not mean that there should be no long-term planning.

All those countries which have adopted the policy of planned development do have long-term budgeting, but these long- term plans do not involve actual using of appropriations for the entire period of the plan by the legislature though it may be called to approve the plan in principles and broad outlines as is done in the case of our Five Year Plans.

7. **Rule of lapse:**

The annuality principle of budgeting also implies that money left unspent during the year for which it was sanctioned must lapse to the Public Treasury and the Government cannot spend it unless re-sanctioned in the next year's budget.

This rule of lapse is essential for effective financial control. If the unspent balance of one year could be carried out for expenditure in future years, it would make the departments independent of the control of the legislature till the time their accumulated balances are spent. But this rule is defective from the point of view of economical planning of expenditure.

The departments, knowing that if they do not utilize grants, they shall lapse, have no incentive for economy and therefore, towards the end of the financial year, they spend it lavishly with scant regard to its urgency or utility.

In our country, the Central and State Governments can constitute reserves or reserve funds, either by allotment of sums from the revenues of a year or series of years or from grants of contributions made by other governments and outside agencies, "with the object of expending the moneys accumulated in the funds on the specific and particular purposes for which they have been constituted."

While the general principle of 'rule of lapse' is accepted as a matter of policy, the Finance Ministry has assured, time and again, the Administrative Ministries that wherever grants have not been used to the full extent for valid reasons, the Finance Ministry would be prepared to consider proposals to allot provision for the unexpended amounts either in the original budget of the coming year or by means of supplementary grants in that year provided the purposes for which these amounts were originally included in the sanctioned grants continue to be operative.

It is hoped that with this assurance the Ministries concerned would take positive steps to prevent the rush of expenditure in the closing months of the year, and also to refrain from making purchases in a hurry merely to avoid lapse of grants.

8. **Treasury control:**

The legislature authorizes the government to spend money but it does not direct them how to spend it. That is the job of the government itself.

The best system of direction and internal control can be seen in the working of the British Treasury in England where it concerns itself not only in regard to the preparation of budget but also exercises day-to-day supervision over the flow of finances to the operating agencies. Through its power of sanctioning money and employment of personnel, it has come to exercise managerial control over the operating departments.

9. **Executive discretion:**

The Executive must be given sufficient discretion in the matter of allotment of appropriation if it is to exercise supervision over the activities of the spending departments.

M. Rene Stourum has rightly said:
"The pilot in-charge of steering a vessel is the only competent judge of the position and of the speed be has need to give his sails because he alone is

posted in such a way as to know the force and the direction of the winds and the currents, which may hinder or delay his movement."

The legislature should provide for broadly defined functions of the spending agencies and the executive should be left alone in the matter of determining the precise means of operation to achieve the purpose set forth by law. It should possess the power to make re-appropriations from one minor head to another.

It should also have the power and means to meet financial emergencies. The provision of a Contingency Fund in India in the name of the President to meet financial exigencies is a fine example of executive discretion.

10. **The form of estimate should correspond to the form of account***:*

This principle means that the budgetary heads should be the same as those of accounts. This facilitates budget preparation, budgetary control and the keeping of accounts.

11. Revenue and capital parts of the budget should be kept distinct:

This principle means that overall surplus or deficit may be found out by taking both into account.

12. Single budget:

Lastly, it is also an important principle of Budget making that the government should have a single budget incorporating all revenues as well as expenditures of the government. A single budget presents to the people a clear-cut picture of the financial transactions of the government as a whole.

But if there are a number of department-wise budgets, some of them may show a surplus and others a deficit. It will not thus be possible to know the net financial position of the government as a whole except by complicated calculations and adjustments.

On the basis of this principle, it is also wrong to prepare 'Extraordinary Budgets' for special purposes. An exception to this principle of unity of Budget is, however, sometimes made in some countries including India when separate budget is prepared for commercial enterprises such as Railways.

India has had a separate budget for Railways since 1924. The Railways are free to keep their profits for their own development after they had made their own contributions to the general revenue. Since 2017, India too have a single Budget called General Budget.

According to Dimock, the important Budget principles are publicity, clarity, comprehensiveness, unity, periodicity, accuracy and integrity. By publicity is meant that the budget should be made public and that there should be no secret session to consider the budget.

The principle of clarity means that the budget should be clearly understandable. Comprehensiveness means that it should give a complete picture of government revenues and expenditures.

One should be able to know the entire financial position of the government. By unity is meant that all government receipts should be consolidated into one general fund for financing all expenditures.

Periodicity means that the appropriations should be authorized for a fixed period and if money is not utilized within that period, it should either lapse, or should be re-appropriated. Accuracy means that the budget estimates should be based on accurate data.

The principle of integrity means that the budget should be implemented as enacted. There should be no departure from it. The above are the principles which are generally followed in every country with some minor differences of details.