



[ASSIGNMENT 2: INTERNATIONAL HOTEL FINANCE MANAGEMENT]

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Executive Summary

Zero-based budgeting is a technique used for developing annual budgets that complement the budget planning and review process. Zero-based budgeting allows top-level strategic goals to be implemented into the budgeting process by tying them to specific functional areas of the organization. Due to its flexibility, this method of budgeting allows department heads to identify alternative ways to utilize limited resources through a systematic review.

A zero-based budget starts from a "zero base" and every function within an organization is analysed for its needs and costs—all expenses must be justified. The budget is built based on the needs for the upcoming year, regardless of whether the new proposed budget is higher or lower than the previous one. Once developed, the budget is balanced given funding constraints. Zero-based budgeting is a method of budgeting in which all expenses must be justified and every function within an organization is analyzed for its needs and costs. The purpose of the ZBB analysis is to assess a particular program's activities against its statutory responsibilities, purpose, cost to provide services, and desired performance outcomes. Some of the advantages of ZBB are that it:

- Facilitates efficient allocation of resources, as it is based on needs and benefits rather than history.
- Drives managers to find cost effective ways to improve operations.
- Increases staff motivation by providing greater initiative and responsibility in decision-making.
- Increases communication and coordination within the organization.
- Identifies and eliminates wasteful and obsolete operations.
- Requires programs to identify their purpose and their relationship to strategic goals.
- Helps in identifying areas of wasteful expenditure, and if desired, can also be used for suggesting alternative courses

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1. Introduction

Zero-based budgeting (ZBB) is nothing conceptually new, is not a budgeting process, and is not “reinventing the wheel.” It is, however, a management approach, and it can be a key decision-making tool for the chief executive officer (CEO).

The term “zero-based budgeting” was launched into vogue by former President Jimmy Carter, who installed the process while governor of Georgia and who attempted to install it throughout the federal government.(Kesmodel, 2015) However, the process was developed in industry, at Texas Instruments, and is currently being used by industrial companies.

There are several key characteristics about the process in its application to date:

- The decision to implement ZBB is usually made by the CEO or other key operating managers, not by the vice president of finance or the controller.
- It is being used by companies noted for their good management. (“Good management is always looking for better decision-making tools.”)

- The process is difficult, requires a great deal of effort to implement effectively, and may be perceived as a threat by many managers. It has failed in a few organizations and is no panacea, yet most companies have found that the benefits far outweigh the costs of implementation.(“Handbook of Budgeting,” 2018) (*What Is Zero-Based Budgeting (ZBB)? Definition, Characteristics, and Stages - Business Jargons*, n.d.)

2. Zero Based Budgeting

2.1 Zero-based budgeting

Zero-based budgeting is a technique used for developing annual budgets that complement the budget planning and review process. Zero-based budgeting allows top-level strategic goals to be implemented into the budgeting process by tying them to specific functional areas of the organisation. Due to its flexibility, this method of budgeting allows department heads to identify alternative ways to utilise limited resources through a systematic review. A zero-based budget starts from a "zero base" and every function within an organisation is analysed for its needs and costs—all expenses must be justified. The budget is built based on the needs for the upcoming year, regardless of whether the new proposed budget is higher or lower than the previous one. Once developed, the budget is balanced given funding constraints.(Pyhrr, 1973)

2.2 Advantages of Zero-based budgeting over Traditional Based

Traditional budgeting is truly out-dated. And other than becoming a simplistic process, it doesn't serve the company, a business, or even an individual.

Not only is traditional budgeting simplistic, but it's also very time consuming because it involves a lot of spread-sheets. And chances of errors are even more in using this method. On the other hand, zero-based budgeting ensures cost-effectiveness and

detailed-orientation, which help a business generate more profits and an individual save and invest more money.

Without a tinge of doubt, zero-based budgeting is a far superior approach than traditional budgeting. (Mukhopadhyay, n.d.)(Kagan, n.d.)

2.3 How the Organisation Might introduce Zero-based Budgeting

The zero-based approach requires each organisation to evaluate and review all programs and activities (current as well as new) systematically, to review activities on a basis of output or performance as well as cost, to emphasise manager decision making

first, number-oriented budgets second, and to increase analysis. However, it should be stressed that ZBB is an approach, not a fixed procedure or set of forms to be applied uniformly from one organisation to the next. The mechanics and management approach differed significantly among the organisations that have adopted ZBB, and the process must be adapted to fit the specific needs of each user.

Although the specifics differ among organisations, there are four basic steps to the zero-based approach that must be addressed by each organisation:

1. Identify decision units.
2. Analyse each decision unit in a decision package.
3. Evaluate and rank all decision packages to develop the budget request and profit and loss statement.
4. Prepare the detailed operating budgets reflecting those decision packages approved in the budget.(GREGORY, n.d.; "Handbook of Budgeting," 2018)

3. Conclusion

The zero-based approach is not a panacea and is not without its problems. The major the problem is that many managers feel threatened by a process that evaluates the effectiveness of their programs. The zero-based process also requires a great deal of effective

administration, communication, and training of managers who will be involved in the analysis. Managers may also have problems in identifying appropriate decision units, developing adequate data to produce an effective analysis, determining the minimum level of effort, ranking dissimilar programs, and handling large volumes of packages. For many programs, work-load and performance measures may be lacking or the program's impact may not be well defined so that the analysis will be less than perfect. Therefore, ZBB should be looked upon as a longer-term management development process rather than a one-year cure-all.

If done properly, the zero-based approach is not subject to the gamesmanship one might anticipate. The traditional budget approach offers maximum opportunity for gamesmanship because current operations are seldom evaluated, and many discrete decisions are never explicitly identified and get buried in the numbers. However, the

zero-based approach removes the umbrella covering current operations and requires managers to identify operating decisions clearly. In ZBB, the most obvious forms of gamesmanship would be to avoid identifying reasonable alternatives, to include the pet projects within the minimum-level package, and to rank high-priority programs low in order to obtain additional funding. If the decision packages are formatted to display the alternatives considered, the workload and performance data, the descriptions of actions, and enough cost data so that discretionary items cannot be built into the cost estimate, it becomes very obvious when such gamesmanship is attempted. Also, because the entire ranking of decision packages must be displayed, it is very easy to challenge a high-priority item that received a low ranking or a low-priority item that received a high ranking.

The problems in implementing ZBB are not to be minimised. The specific needs, problems, and capabilities of each organisation must be considered in adapting the approach. Although most of the basic concepts of the approach have been maintained, the specifics of administration, formats, and procedures have been different for each organisation that has adopted the approach. ZBB can be applied on an intensive basis throughout all levels of an organisation, only to selected programs, or only at major program levels rather than involving all operating managers. The strategy of implementing the zero-based approach must be developed for each organisation, depending on its specific needs and capabilities.

Top management must play a major role in implementation. Because the process is difficult, managers must stand behind it, understand it, and use it. Finally, managers must be willing to make the tough decisions and trade-offs that the process requires.

4. Budget Calculations

- List out income
- Tally up expenses
- Create budgeting categories for absolutely everything
- Put those dollars to work
- Track your expenses & stay flexible

5. Reference List

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