

MANAGEMENT ACCOUNTING

LCBB5002

Assessment 1

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INTRODUCTION

This project shall be highlighting the technique of budgeting which is used by the managers in the decision-making process of the organization. It shall show how various budgets are prepared which can be utilized for proper allocation of resources, future profitability, and growth prospects. It shall demonstrate the various budgeting styles like the activity-based budgeting, zero based budgeting and the incremental budgeting and its merits and demerits posed on an organization. It shall also be disclosing the most suitable style of budgeting that can cope up with the changing environment. It shall be explaining the static and flexible budgeting and its uses in different types of situations. Lastly the report shall be describing the participative budgeting and the pros and cons of applying it in an organization.

Budgeting

Budgeting is a technique that is used by the management to formulate a successful business plan describing where we are and where we want to be. The budgets are formulated with the help of business plans and it shall disclose the level of activity that is to be undertaken to generate the desired profitability and growth for the company. Budgeting facilitates the controlling function of management enabling to compare the actuals with the budgeted and determining the level of deviations (Barasa and et.al., 2017). It shall prove to be helpful in proper allocation of resources, assigning the roles and responsibilities, determining goals and objectives and its achievement.

Budgeting used for decision-making

The various budgets that are prepared can serve as the backbone of the company and shall be facilitating the short term and the long-term decisions of the company. It shall act as a blueprint for conducting the various activities in the business. There are certain major decisions that can be facilitated by the preparation of the budgets like the determining the short term and the long-term financial decisions, ascertaining the need and the availability of funds, deciding the hierarchy and division of the roles among the employees etc (Bogsnes, 2016).

The short term and the long-term goals are ascertained and accordingly the activities are planned like the inventory management, cash flow management, capital budgeting decisions etc. Such an act of governing short- and long-term goals shall be providing clarity and direction to the subordinates.

Ascertaining the need and the availability of funds is another decision that is taken with the help of budgets that are describing the operations to be carried in the future. Proper cash management is very necessary so that no idle money is maintained, and all the operations can be carried on smoothly and efficiently (Hijal-Moghrabi, 2019).

The roles shall be divided in the subordinates based on level of operations only, which is disclosed in the budgets. If proper assignment of the duties is done than it shall help in avoiding wastages, repetition of work and overcrowding which decreases the efficiency of the workforce.

Budgeting styles and its merits and demerits

There are four different types of budgeting styles like the zero-based budgeting, activity-based budgeting, incremental budgeting, and the value proportion budgeting. Different styles are used by different organizations based on the environment they operate in and the nature of the business (Ibrahim, 2019). These styles are used by the management to design the various budgets like cash budget, operating budget, income, and expenditure budget etc.

Zero based budgeting is a style of budgeting wherein the company formulates the budgets from the scratch without using previous year's data as the base. This is a highly effective method of budgeting wherein all the costs and the expenses are undertaken with proper justification so that all the discretionary costs can be addressed. The allocation of the resources shall be prioritized based on the priority of the operations of the business (Miller, 2018). This style is majorly used when the company is being restructured. Its merits can be that it avoids all the discretionary costs, involves justified expenses, shows true profitability, focus on the cost benefit analysis, appropriate allocation of resources. The major demerits can be namely time-consuming, skilled workforce requirement, leads to conflicts and rigid in nature.

Activity based budgeting is a style wherein the top-down approach shall be used to frame the budgets. In this approach firstly the targets or goals that are to be attained shall be identified, based on those targets the level of operations shall be governed. Then the cost drivers for these activities shall be analysed and shall be incorporated in the budgets. In this also the past year data is not utilized but the current objectives shall be considered (Popesko and Socova, 2016). The merits of forming budgets using this style shall be that it shall connect the business goals with the business activities performed, better control on the operations, proper estimations regarding the revenues and the expenses and the allocation of resources. The demerits can be that it involves higher cost in its implementation, technical skills are required, and assumptions can be improper.

Incremental budgeting is a method of budgeting in which the past year's budget is the base and changes are made according to the desired result for the current year. The additions and subtractions shall be done in the revenues and expenditures of the last year as per the requirements and shall be presented in the budget. It does not include the in-depth analysis and so major elements in the business get ignored (Rubin, 2019). The advantages of preparing budgets using this style can be the process is easy, requires less skills and expertise and can be used in a less changing environment. Whereas the demerits of such method can be that it ignores the changes in the external environment and discourages innovations and flexibility.

Suitability in the changing environment

The most suitable style of budgeting in the changing environment and to compete and sustain in the competitive environment can be the activity-based budgeting. As the activity-based budgeting shall align the operations of the business with the plans and objectives, it shall help in maximizing the profitability and growth prospects of the business (Usman and Usman, 2016). Since in this method of budgeting the company shall be firstly designing the goals and then coordinating the operations and the cost with it, so it shall prove to be essential

in controlling the activities. It shall also help in proper estimation of the revenues and expenses of the business avoiding unnecessary wastages.

Static and flexible budgeting

There are different types of budgeting styles which are being utilized by the organization based upon the needs and requirement. Pertaining to the change in the technological environment, it is important to effectively evaluate the use of the budget types and how it will be helpful for the businesses. There are mainly two major forms of budgets one is static budget, and another is the flexible budget. The static budget is generally used as the projecting tool for the purpose of estimating the business expenses with the given time frame (What is a static budget? 2020). In case of any discrepancy in the outcome, it will result into budgeting errors called as the static budget variance. The amount under this, does not change with change in the volume. For example, the annual budget of the company is static which states that the sales commission budget expense will be \$200,000. Therefore, the sales commission expense budget will remain the same irrespective of actual sales being \$2 million or \$4 million. In contrast to it, the flexible budget works better in performance evaluation. This budget adjusts with the change in the volume as against the static budget. This can be explained with help of an example, in the above example, under the flexible budgeting, the sales commission expense might be expressed as 5 percent, which easily flexes with the changes in the sales volume (What is a flexible budget? 2020). Thus, when the sales are \$2 MN, the commission expense will be \$100,000 and the similar way, \$4 MN will account for the \$200,000. Therefore, both the types of budgets are being utilized by the organization in meeting with the technological changes.

Participative budgeting with pros and cons

The participative budgeting accounts for the involvement of the lower-level management in the budget preparation process. This form of budgeting has the merits of transferring information from upward along with increasing the motivation level of the employees as they are being involved in the budget process (Gavrilova, 2018). This also helps in aligning the company's goals with the personal goals of the employees which helps in accomplishing of goals in a better way. On the flip side, it has certain disadvantages as well, like it is a time-consuming process as the budget is prepared from the lower to the top management which involves too much participation which may result into derail of the process. There are chances that the employees might under/overestimate the figures to manipulate the budget.

CONCLUSION

Therefore, it can be inferred from the above that the use of the technological advancement has resulted into undertaking prompt and real time decisions which requires the organization to prepare budgets and plan on a short-term basis. This is important in case any change is required to be implemented on an immediate basis. The static and flexible budgets are being used by the organization so that it can effectively work on meeting with the set objectives and target but because of uncertain event, it can make relevant changes in the budget through flexible budgeting and, it can use the participatory budgets for enhancing the performance and productivity.

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