

UNIVERSITY OF WALES TRINITY

SAINT DAVID

COURSE: BUSINESS MANAGEMENT

**MODULE: MANAGEMENT
ACCOUNTING**

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1.0 Introduction

Every business which exist currently do accounting to identify financial transactions. Whether the business is large scale or small, to find its exact income and expense it has follow accounting. In this financial process (accounting) budget plays a major role and it's considered one of the most important factor in strategic decision making. Budget is considered as a financial plan that are to be undertaken by every business in their future implements. Each organization got its own budget according to the asset and expenses it owes. In past all organizations followed the similar way in doing budget but now it transform into modern budgeting system and many organizations come up with their own way of budgeting process which mean implementing new ideas and fractions that makes easy for them do financing.

This report shows a clear view on budgeting and why it's important for an organization to prepare budget. Making a budget is a huge task for a management, especially long term budgets must be accurate as it will be a high impact in strategic decision making of a company. If the budget is not accurate or shows false information, definitely then the high level decisions will go wrong and result in company's failure. Further in modern budgeting, balanced scorecard and activity based costing are huge measures for any kind of business or industry to find out their position. It also helps the organizations to get prepared to face future complements and degrades as well.

2.0 Budgets

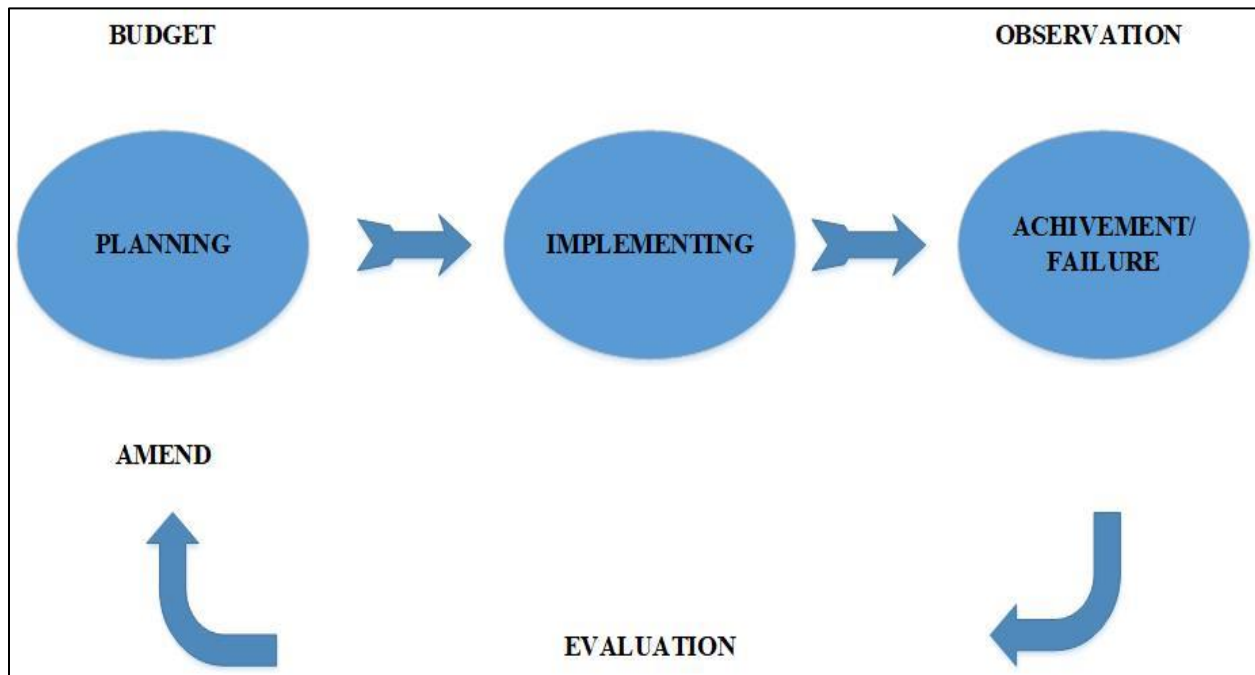
Simply definitions says that budget is an application done for financial purposes but in real it's not simple as it articulates. In companies high level managers put their complete effort to bring out accurate budget for a company. Because budget is the complete financial plan that decides organization's achievements towards financial and operational goals. In depth it can be said as budget is the blue print for an organization's strategic plan. A proper budget will handle the company's resources in an efficient way to get maximum output.

Budget gives a clear view for a company to move forward with available resources towards the success. It helps the management to supervise whether the resources are utilized in proper way and the time ranges. When a proper budget plays in strategic decisions means the company is competing well with its competitors. Also a budget helps the management to evaluate when there are failures as what went wrong for them to balance accordingly. Each departments in a company will be making their own budget according to future planning finally all departments submits them to high levels of the company, they clarify them and analyze in to 1 whole budget its known as master budget.

2.1 Planning cycle

There are 3 types of budgets according to the time frame it covers, if it's less than 1 year means short term, up to 5 years common and more than 5 years are long term budgets. It's not possible to achieve goals as mentioned in budget all the time. There could be huge failures too, because everything doesn't happen as what we predict. Simply management must amend budgets when there are changes take place in the environment, each and every time management must work on it then only a company can move towards success.

Figure 1 Planning Cycle



The above image shows a clear view on planning cycle in budget. As the first step management must plan and make a sketch on how the available resources should be used. Then it must be implemented after we can find whether it moves towards achievement or failure through observing in the process time to time. Meanwhile management can evaluate on making changes, what are to added to come out with perfect flow in future. Once the decisions made the budget must be amended on time.

3.0 Budgeting process and methods

3.1 Balanced Scorecard

Balanced scorecard is a metric that used by top level management to identify and analyze some of the internal perspectives. Also it helps to understand and study the current situation of the organization and that makes easy to find out ways for the improvement.

Balanced Scorecard is mainly used in strategic decision making by top level management in order to improve the internal factors in the organization as a result it will bring good outcome in external as well. Moreover Balanced Scorecard was found in 1990's by Dr. Robert Kaplan (Harvard Business School) as measurement indicator to look the organization in a deep view and to find out the stability by top level management. Since from that till to date many organizations and industries around the world use this balanced scorecard metric on their strategic decision making.

In order to find the stability balanced scorecard focuses on four perspectives in an organization. Financial, Customers, Internal corporate and Innovation are the four areas look into account in strategic decision making and the balanced scorecard show how these four balanced for future development of the organization. Basically in past balanced scorecard is been used only to measure and identify the four aspect of the organization but in present it gives the main result for making decisions while showing the clear view of the organizations current situation that are to be improved in an accurate way.

3.2 Activity Based Costing

Activity based costing is a tool which allocates the overhead costs of each activities into product and services. All individual activities are been allocated through cost driver. Simply cost driver is a model which contains similar type of factors in the product cycle. For example if we take direct labour and direct material, it's easy to add these costs into the products but the indirect cost cannot be added easily, for that ABC tool uses cost driver in order to add indirect costs through most relevant agent. Simply ABC divide all indirect cost into different categories and make them joint

with relatively familiar group, it's been called as pool. Assuming a toy manufacturing company's accounts, the following sum will give a clear understanding on it:

Step 1

E.g.: Company's overheads are been allocated to relative pool through cost driver as follow,

General Ledger	
Machine maintenance	£10,000.00
Payroll taxes	£16,000.00
Purchasing dept. labour	£30,000.00
Fringe benefits	£24,000.00
Purchasing dept. supplies	£4,500.00
Depreciation	£7,500.00
Electricity	£18,200.00
Unemployment insurance	£19,600.00

Direct Labour A/C	
Payroll	16,000
Fringe	24,000
Insurance	19,600
£	59,600.00

Machinery A/C	
Maintenance	10,000
Depreciation	7,500
Insurance	19,600
£	37,100.00

Purchase Orders A/C	
Labour	30,000
Supplies	4,500
£	34,500.00

Step 2

The above ledger accounts show how the indirect cost are been added into direct cost accounts as pools. Further the following sums will clarify, how the ABC rate is been calculated for each pool.

Assumptions

1. Direct labour hours = 4500
2. Machine hours = 1500
3. Purchase orders = 1000

Activity based costing rates

- $59600/4500 = 13.25$ per direct labour hour
- $37100/1500 = 24.74$ per machine hour
- $34500/1000 = 34.5$ per purchase order

Step 3

Allocating the hours for each product according to the base it use.

Assumptions:

Base	Toy AD	Toy BD	Total
Labour hours	3000	1500	4500
Machine hours	1000	500	1500
Purchase orders	500	500	1000

Step 4

Allocating the overhead to each product using base hours and rates.

Toy AD

	AD Base	Rate	Allocated amount
Labour hours	3000	13.25	39750
Machinery hours	1500	24.74	37110
Purchase orders	500	34.5	17250
Total			94110

According to above table the base hours are been multiplied by ABC rates which gives the total allocated amount of £74,188.05 to be applied for the product AD pool. Same method is followed for product BD as well.

Toy BD

	BD Base	Rate	Allocated amount
Labour hours	1500	13.25	19875
Machinery hours	500	24.74	12370
Purchase hours	500	34.5	17250
Total			49495

The total basic amount of overhead was Direct labour £59,600.00 + Machineries £37,100.00 + Purchasing orders £34,500.00 = **£131,200.00**

According to ABC the amount allocated was AD £94,110.00 + BD £49,495 = **£143,605.00**

It shows variance of £12,405.00 in the above both totals, which means the allocated amount is more than the real amount. In this case the company gets an excess amount at the end and its considered as an income for the company but in case if the allocated amount was less than the real amount then the company will bare that variance as extra expense which is not good the company.

4.0 Conclusion

This report completely gives a clear view on how the budget plays the major role in strategic decision making in business world. Moreover Balanced Scorecard is measure tool to find out the position of the organization is balanced or not, simply like SWOT analysis. Activity Based Costing helps an organization to allocate all the overhead cost of production in order to cover up them in proper and pricing the product. It directly make all overheads to flow into related pool and gives the exact amount allocated at the end.

On my point of view if a management prepare an accurate budget on time, an organization will move smoothly towards its objective. At the mean time management must follow the progression and make amendments according to the changes take place in environment which will affect the business.

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6.0 Appendix

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