



BUDGETING PROCESS

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INTRODUCTION

Various companies use different budgeting for their organisations whether it is for short-term or for long-term depending on the plan they must do. In this study, it will expand our knowledge on how budgeting is needed to improve business plans and the processes in preparing budgets which is important for budget managers to spend on activities to achieve their targets. Also, it will provide explanation on alternative forms of budgeting such as Balanced Scorecard and Activity-based budgeting.

Exploring about this subject gives us a better understanding of how budgeting has a connection with the planning and controlling of an organisation, and how various budgeting has significance with each other. Also, this study will seek to explore the insight of using the traditional budgeting to organisations, including its advantages and limitations.

IMPORTANCE OF BUDGET

Budget can be defined as a record of profit and expenses of activities made by company departments or by making projects, which can be done by months or quarter-years (Francke, 2014). It means that it is used by the management to accomplish tasks in every stage or phase of activities to achieve the organisation's objectives. Hence, Budgeting is the use of resources either raw materials or money either to obtain a target or to supply the needs of human resources. In every department of a company for example, there are budgets allocated for each office to use to function like office supplies, equipment, tables and chairs and electric appliances.

Budgeting are useful in every organisation most especially to the managers of each department who are responsible for the planning and control of funds. Generally, there are 5 advantages of budgeting to managers which were listed by Atrill and McLaney (2013).

- Support future analysis and identify potential short-term threats.
- Manage some areas of the organisation through coordination.
- Influence better performance of the managers.
- Deliver guidelines for operating a system.
- Gives managers an organise authority to utilise in specific boundary.

These uses of budgets are significant in every company in a way that they can plan objectively in the present situation and forecast the future condition. It decreases uncertainty, boost satisfaction of the job, and contribute accurate budget for a target (Lidia, 2014).

Controlling and forecasting are part of business strategies to meet and maintain the objectives after getting the results of the planned action. Planning is the foundation of having a budget, thus, it helps the managers to evaluate how to use budget effectively by spending in a specific margin. Putting budget is a helpful means in organisation and society of formulating a forecast on expenses and aim not to overrun in this area (Heupel and Schmitz, 2015).

Managers control budgets either minimising or maximising the resources given to each area, depending on its needs and what has been planned for the current period. Management and staff will check the execution and achievement of the budgeted values in performing an activity (Lidia, 2015). Therefore, having a good budgetary system, it can help them predict budgets for the next year, which depends on the project they will do in the next period if and only it is accurate for achieving the organisation's objectives.

VARIOUS FORMS OF BUDGET

There are various forms of budgets which managers prepare in the company. All budgets must maintain the goals and operational strategy of the whole organisation by cooperation of all budgets as some budgets depends each other (Marsh, 2012). These budgets are called Master Budget which are the coordination of Sales, Production, Materials, Labour, Variable Overheads and Fixed Overheads. It means, one component must be completed before proceeding to another component.

For example, production department cannot do its task if there is a lack of information from other budget departments like materials, labour, etc. The management can organise business activities using the master budget as it serves as the planning and control tool (Irfanullah, 2013).

Traditional budgeting is an outlined plan of a company, both financial and nonfinancial aspects which is use in the coming period (Horngren, *et al.*, 2012). This process is a financial

outline that fund specific goal and acts as guide to direct and manage business where it involves managing of costs and cash flows which was introduced before. Its main function is to complete the objectives and lead the management in planning, coordinating, measuring and rewarding (Ildiko, *et al.*, n.d.).

According to Borad (2017), this method is easy to implement, there is stability, decentralization and consolidation. It means, it is prepared faster that it can save time and effort because there are only few changes to be made as they take the previous budget as a base for the next budgeting requirements. The old preparation has been used by most organisations before that the organisation knows well the activities to be done. In the aspect of decentralisation, the head department can prepare it and can change within allowed limits. Traditional budgeting can able to combine projects together which can improve performance of other weak performing projects.

On the other hand, there are problems seen on using traditional budgeting. Some of these are inefficiency, low change responsiveness and failure to motivate desirable behaviours. The use of spreadsheet takes up too much time which, it is susceptible to errors of data entries, issues of control versions and problems creating accurate formulas. Reviews are not conducted regularly that it fails to motivate people to encourage their interests in the company. It creates bureaucracy that caused control which made people feel invaluable and sometimes builds barriers among departments (Yvanovich, 2012).

Based on studies, new methods have been introduced due to disadvantages of traditional budgeting that has seen that can affect the performance of businesses. One of the new methods of budgeting is the Balance Scorecard that focuses on the performance of the company to modify strategies. Balanced Scorecard is a performance metric that was introduced in 1992 which is used to identify and improve some internal functions of a business and the result of its external outcomes handled by strategic management (Investopedia, 2017). It measures the performance of a company with the use of 4 perspectives: financial, customer, internal business process and potential (Kaplan and Norton, 1992 cited in Zizlavsky, 2014).

These are the indicators to know if the business is doing well its performance both financial and non-financial. BSC drives managers to realise that the company is fully organise and

supports the management to attain business' goals in one section without affecting the other area by indicating the targets and results from several perception (Pietrzak, *et al.*, 2015). Meaning, the vision and mission of a business can be acquired through better managing of the 4 areas.

The challenge of most organisations is the measurement of innovation because mostly, it needs to track the intangible assets (Ivanov & Avasilcai, 2014). Measuring some of the areas involve in each department such as, the Return on Investment, cash flow, number of activities per function, employee turnover, job satisfaction, learning opportunities, customer satisfaction rate, and delivery performance to customer, can be improved once it is analysed by its results which are useful for strategic plan for long-term success.

Balanced scorecard has equal aspects in the business, both internal and external (Gomes & Romao, n.d.) The involvement of non-financial aspect can determine the customer's demand. For example, the needs and wants of consumer in psychological way can be discerned through trends. Therefore, the company can make plans for better products or services to produce that can affect the budgeting.

However, in some cases, non-financial performance is not accurate and effective to business planning because of its qualitative aspect that can give incomplete information. A quantitative link cannot be established between non-financial leading indicator and expected financial results as it is difficult to predict, and numerous factors may impact the result (Molleman, n.d.). This can affect the decision making of an organisation because mostly when analysing, they used quantitative analysis to interpret things such as statistical reports rather than interpreting unquantifiable data.

Another approach in budgeting that existed was the Activity-based Budgeting (henceforth ABB) which was developed from activity-based costing. Activity-based costing has a primary type of method to find, and decrease alteration of the allocation of indirect costs that obtained in traditional system (Stefano & Filho, 2013).

ABB is a method of estimating costs through allocation of resources by the activities needed to produce a product or services, and a method to measure both the cost and performance of the activities and cost objects (Almeida & Cunha, 2017). This is different from traditional budgeting where annual budgets were created from adjusting the level of existing cost. ABB

focuses on types of activities, its expected size and the resources needed to be utilised (Pietrzak, 2013). For example, when an organisation makes an activity to develop their product, the spending will be reviewed and allocate the budget to the prioritised department that do the activity.

There are 2 stages involve in ABB (Hansel et al., 2003 cited in Cardos, 2014)

- Operational loop activity-based – ABB method is applied between the available sources and spending of supplies of the activities once they are known to meet operational stability.
- Financial loop – expenses are identified after knowing the requirements, activities, and capitals and supplies.

From the concept of ABB and the traditional budgeting, ABB is far better method to use when creating a budget because it specifically identifies what are the resources needed which it will give organisation a better planning that is more accurate than just adjusting the cost of the previous budget made. To forecast the required for activities and usage of resources to manage them, knowledge is used in ABB (Hanninen, 2013). Costs of different activity can be categorised and control which it can be changed easily if there are changes made.

CONCLUSION

Budgeting is important in any organisation as it is part of strategic planning to control their finances by spending it to pay for the expenses and resources. As understood, every department in an organisation prepares budget account and through coordination with each other, they are managed into one which is called as Master Budget.

Meanwhile, different budgeting process is being used and adopted by various companies and they are identified and compared. It shows that Traditional budgeting is oldest method being used and found its disadvantages to companies for it is not effective for long-term goals. That is why, modern methods are introduced such as Activity Based Budgeting and Balance Scorecard. Both are good to adopt but it depends on way it is being used to. One of these methods can be helpful in decision making of a company for successful business strategy.

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