BUDGET, BUDGETING AND BUDGETARY CONTROL

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Absract:

Budget, budgeting and budgetary control are managerial tools for controlling economic transactions and other resources within an organisation. Basically, these terms were used by a government or a governing body for a nation's financial planning. Similarly, these concepts- were used by monarchs and rulers of different countries in past for their economic transactions and futuristic planning of their countries. After the World War I, the significance of budget, budgeting and budgetary control increased to a greater extent. Every profit-making and non-profit organization makes plans in advance regarding its financial activities for the financial year. Since ages till the present times economic activities of a nation or an organisation are controlled by budget, budgeting and budgetary control. As time passed, these concepts became more elaborate and precise. Even for assessing the non-monitory activities, these concepts were applied. In the era of Globalization, the economic activities of the world became faster and clearer. The domains of Accountancy and Costing demanded more precise ideas regarding budget, budgeting and budgetary control. With the advent of Industrialization and Commoditization, the importance of accounting and costing increased and so also of budget, budgeting and budgetary control in every organization. Even the non-profit organizations started considering seriously their budget, budgeting and budgetary control. These concepts, in the post-globalization era, have emerged with wider perspective. Scholars and managers in the arena of Accountancy and Costing are using these concepts to micro activities like activity based budgeting and performance based budgeting. Further, these concepts are applied to departments and activities individually and independently. The present paper attempts to capture the use and application of the concepts of budget, budgeting and budgetary control in the changing scenario of accountancy and costing.

Key Words: *Budget, budgeting, Budgetary control, Managerial tools*.

In the domain of accountancy and costing budget, budgeting and budgetary control are the key terms with which almost all-monitory and non-monitory activities are governed. The terms 'budget,' 'budgeting' and 'budgetary control' are not new ideas that have emerged recently. These concepts have been used by people in their day-today transactions as well. The literature from the past till the present generation has been using the same for the economic activities of an organisation as well as of any governing body. The present paper is an attempt to trace variant aspects and scope of budget, budgeting and budgetary control that are used by writers and scholars in their writings. ‘Budget,’ ‘budgeting’ and ‘budgetary control’ are concepts traceable to the biblical days, precisely, the days of Joseph in Egypt. It was reported, “Nothing was given out of the treasure without a written order.” This indicates that budget, budgeting and budgetary control can be seen as written records maintained by a ruler or a governing body. The Egyptian king, Joseph made the provision of food grains for the country which lasted for seven years during food crisis. This instance is evident to understand the existence of budget, budgeting and budgetary control during the ancient days.

From the dawn of human civilization on the earth and since the transactions between two persons, or since the evaluation of income and expenditure, the concepts budget, budgeting and budgetary control systems must have been prevailing in the human mind in the ancient civilizations of the world, regardless of their nationality and language. Hence, one needs to trace the emergence of the word ‘budget’ in literature available. The term ‘budget’ is derived from a French word, ‘bougette’ meaning a ‘small bag’. Further, the use of the word spread to England, where it came to designate the leather bag in which ministers of the crown carried financial plans to parliament, and eventually it became synonymous with its contents. Similarly, the use of the word in England, now, refers to the spring financial statement, which focuses on measures of taxation. In most countries, the term refers to the annual expenditure and revenue plans tabled in the legislature. The first traceable legal definition of budget is contained in a French decree of 1862. It chronicles, “The budget is a document which forecasts and authorizes the annual receipts and expenditures of the State.” [1] This definition, though narrow in its arena, paves the path for other writers to use and develop it further. It also makes clear that budget is a government document which forecasts the annual receipts and expenses of a nation.

With the outburst of World War I and its aftermath, budget was introduced for the first time as a formal tool to manage costs and cash flows in large industrial organizations. Similarly, after the World War II, industrialization reached to its height. As profit making and meeting the contingencies became a more conscious effort, the industrialists thought more seriously about these concepts and their applications in their factories and organisations. In other words, budget or budgeting was a tool used by the factory owners/industrialists/organizers to control laborers, funds and other resources as well.

Johnson, one of the scholars, states that it was during 1960s companies began to use budgets to dictate what people needed to do. Further, in 1970s, performance improvement was based on meeting financial targets rather than effectiveness in the performance. Budgeting, in business organizations, is formally associated with the advent of industrial Capitalism for the industrial revolution of the eighteenth century, which presented a challenge for industrial management.

Budget is a financial planning of an organisation set in advance to achieve a desired goal. To ascertain this idea one needs to trace the concept in a broader sense captured by ICWA in *An Introduction to Budgetary Control, Standard Costing, Material Control and Production Control* (1950) which defines budget as, "a financial or quantitative interpretation prior to a defined period of time, of a policy to be pursued for that period to attain a given objective." [2] This definition interprets budget as a quantitative interpretation set in advance to attain an objective. The objective is already given and accordingly, the financial interpretations are made. It is a policy to be followed to achieve a given target.

Gareth Morgan in his book titled, *Images of Organization* (1997) considers budget as not merely a financial tool but the most powerful managerial tool, a management can use for making sure that key resources, especially performance resource are assigned to priorities and to results. According to him budget is, "a tool that enables the manager to know when to review and revise plans, either because results are different from expectation or due to environmental, economic conditions, market conditions or technologies change, which no longer correspond to the assumptions of the budget." [3] Morgan emphasizes that budget should be used as a tool for planning and control. He considers budget as the prime tool with the management with which it can inspect, survey, change the policies of the company according to the changes in the market, changes in the economy or changes in the technology.

Further, The Tennessee Board of Regents (2006) in the board meeting goes a step ahead and, explores and investigates into this domain bringing the minutest possible thing covering budget. The Tennessee Board of Regent ruminates:

> *Budgeting as the process whereby the plans of an institutions are translated into an itemized, authorized and systematic plan of operation, expressed in Dollar for a given period. Budgets are the blueprints for the orderly execution of program plans; they serve as control mechanisms to match anticipated and actual*

revenues and expenditures. It is the control mechanism aspect of budgeting that is the focus of this policy.[4]

This definition focuses more on the operational plan expressed in terms of money. Further, according to this definition budget is essential for an orderly execution of the plans and also for comparison between the actual and the budgeted performance of an entity.

As time passed, budget becomes all enveloping as it takes into account the aspect of decentralization which indicates that decision making is allocated to different levels of management. In C*ost and Management Accounting*, (2006) the author, C. Drury explicates, "budget serves as a vehicle through which the actions of the different parts of an organization can be brought together and reconcile into a common plan by compelling managers to examine the relationship between their own operations and those of other departments, and to identify and resolve conflict in doing so." [5] He pinpoints that through budget the top management communicates its expectations to lower level management, such that, they coordinate their activities toward attaining those expectations. The definition also brings out the importance of decentralization in an organisation for the successful budget which indicates that budget also covers non monitory aspects of the personnel and management.

Further, one has to look into the advanced use of budget and budgeting. Neely, A. Bourne, M. and Adams, C. (2003) in their scholarly article entitled, "Better Budgeting or beyond Budgeting? Measuring Business Excellence" examine the weaknesses of the traditional budgetary practices and make an in depth investigation in the concept of budgeting. They investigate the concept and make it more elaborate as well as micro-based. They ruminate:

Five different classes of budgets that fit these criteria; activity based budgeting, zero based budgeting, value budgeting, profit planning and rolling budgets and forecasts. Activity Based Budgeting is similar to Activity Based Costing and Activity Based Management. It actually involves planning and controlling along the lines of value adding activities and processes. Resource and capital allocation decisions are consistent with Activity Based Management analysis, which involves structuring the organization's activities and business processes so that they better meet costumers and external need. Zero Based Budgeting, *expenditures must be re-justified during each budgeting cycle rather than basing budgets on previous years or periods. Zero based budgeting is not built on inefficiencies and inaccuracies of previous history.* [6]

This modern definition has a wider acceptability as it covers almost all possible aspects of budget, budgeting and budgetary control in modern times. Similarly, the authors state that budget provides the standard by which performance would be judged. Budget is the operating plan of the organization for the period it covers. It provides financial information which enables management to keep cost at a minimum and preserve working capital. Budget control system enables operations to be planned in advance over a fixed period by preparing estimates of fixed and variable expenses, sales and working capital. Budgetary control educates personnel in making the most effective use of facilities that are available with the organisation.

Subsequently, one needs to examine the concept of fixed budget as it is a kind of budget. A budget which is nonreversible and cannot be changed easily is known as fixed budget. G.H. Hosfsede (1967) in *The Game of Budget Control* explores the concept as, "Fixed Budget is therefore a budget which once made and accepted cannot be changed for whatever reason being that fixed cost are incurred and still persists irrespective of sales volume." [7] This definition looks upon the fixity of the budget as its cannon.

Similarly, the other pole of fixed budget is flexible budget. In order to mould and modify the policies of an organisation, it is necessary to adopt flexible budget. Li Xiaobei and Dai Shengli (2011) in their research paper titled, "Research on Flexible Budget of Marketing Expenditure School of Management," expound, "The flexible budget is founded on the basis of cost behavior analysis. According to the dependence relationship among portfolio, cost and profit, the variable cost and fixed cost can be distinguished and the correlative budget methods can be set down based on each kind of foreseeable professional competence." [8] This definition stresses the accommodative capacity and character of budget which according the changes in circumstances is modified by the management. Accordingly, such budgets help the organisation to adjust as per the need and demand of the time.

As compared to budget, budgeting is a wider concept as it envelops a series of budgets and an array of programmes. It is a process within a specified period of time which deals with the projects and programmes of an organisation. It deals with a number of budgets and financial decisions of an organisation in a specified period of time. In his resourceful book entitled, *Managerial Cost Accounting* (1977) Gordon Shillinglaw, chronicles:

> *Budgeting is an integrated set of project and programmed decisions covering the organisation as a whole, and each of its many parts to a specified period of time. In a big organisation budgeting involves lot of work requiring the setting up of a separate budget organisation. In an organisation, the budgets have to be drawn at the departmental and divisional levels. Central finance wing has the responsibility of reviewing and integrating the budget into organisation wise plan which will be further consolidated for the purpose of implementation at different levels in order to achieve the overall objectives of the organisation. A budget organisation is necessary because the budget has an organisational dimension concerned with the different action levels in the organisational structure, viz. at the departmental, divisional and institution levels.* [9]

To add to this, the 1970s comes out the novel concept of Zero-Base Budgeting. It does not deal with adjustments as they are done in traditional budgeting. Generally, it begins with zero and closes with a zero too. This concept is more poignant and annual result oriented as it does not compare the performance of the present year with the output of previous or preceding year. The study material, *Zero-Based Budget briefing* the CIPFA (2006) attempts to trace the definition of the concept of Zero-Based Budgeting as "the preparation of operating budgets on the assumption that the organisation is starting out afresh in the new planning period it as is the life of the organisation exists as a series of fixed-term contracts. The key benefit of a zero-based approach is that it focuses attention on "the actual resources that are required in order to produce an output or outcome, rather than the percentage increase or decrease compared to the previous year." [10] This concept makes clear that Zero –base budgeting is a point at which an organisation begins afresh.

In the modern era of globalization, budgeting has become so pointed and sensitive that it brings micro elements like activities into budgeting. Activity based budgeting is like zero-base budgeting with the only difference that zero-base budgeting begins with zero, whereas the later begins with a separate activity. This indicates that budgeting is segregating it budget and budgeting on the basis of activities conducted within an organisation. Also, this kind of budgeting facilitates delegation of authority and liberty in decision making. Maddox, the author of *Budgeting for Not-for-Profit Organizations* (1999) enunciates, "Activity-based budgeting is an outgrowth of activity-based costing, which is similar to zero-based budgeting. This budget type accounts for how staff members allocate their effort among activities. Once the full cost of each activity has been calculated, drivers can be established that link support activities to the primary activities of the organization in a law enforcement environment the primary activities are the direct costs of program delivery." [11] Each activity, therefore, gets linked with the other and so also the costing of each.

The modern corporate world comes out with a further advanced idea like 'Participatory Budgeting' which propagates democratic atmosphere in preparing budget. Each human factor contributes in the preparation of budget. Every bit of information related to budgeting is contributed by the managers. In *Journal of accounting research* Kanodia, (1993) in his paper titled, "Participative budgets as coordination and motivation devices" posits, "participative budgets emerge endogenously as an optimal co-ordination mechanism when unit managers share their private information about their operating environments with the superior in order to have an optimal budget allocation. Such participative budgets can contribute to internal task understanding, help co-ordinate functional activities and provide a benchmark for skill and knowledge, against which subsequent performance can be evaluated." [12] This definition emphasizes the functional activities and coordination between different departments and individuals in an organisation. It also highlights the monitory reward or perks to the managers on the basis of the achievement in the unit which suits to the cut throat competition of the corporate sector.

The late 1990s showcases the modern concepts like Performance Based Budgeting which focuses the efficiency, effectiveness and productivity of a plan. The aspects like inputs, outputs, performance and efficiency are also covered by this definition which makes budget, budgeting and budgetary control more poignant. M. Andrews (2004) in his article captioned, "Authority, Acceptance, Ability and Performance-based Budgeting Reforms" states Performance-based budgets need to contain information on the inputs (measured in monetary terms); outputs (units of output); efficiency/productivity data (cost per activity); effectiveness information (level of goal achievement). These performance objectives are then integrated with budget preparation to allow for the alignment of spending plans with performance reporting at the time the budget process is initiated. At the end of each budget period performance-based audits can be completed, which measure the results of programmes using the same performance measures produced in the budgeting process." [13] Similarly, performance budgeting refers to procedures or mechanisms intended to strengthen links between the funds provided to public sector entities and their outcomes and/or outputs through the use of formal performance information in resource allocation decision making. Formal performance information in this context refers to performance measures, measures of the costs to particular parties of outputs and outcomes, and assessments of the effectiveness and efficiency of expenditure obtained through the use of any of a range of analytic tools. The core objectives of performance budgeting are enhanced allocative and productive efficiency in public expenditure.

Budgetary control, in the modern times, is an effective tool used by the management to control the employees and turnover in the organisation. Budgetary control deals with decentralization of authority. It is essentially a management tool whereby upper management can decentralize responsibility to lower levels but retain centralized control. Therefore, costing and budgetary control systems are closely linked with each other. Similarly, budgetary control also functions as a system that has certain inputs and outputs in an organisation. This scientific approach is brought forward by Gerard Hofstede (1967) in his book, *The Game of Budget Control* views, "the budget control process as a system with certain inputs and outputs. The inputs of a budget system include loose or tight standards, process of participation in standard setting, quantity and quality of communication about budget performance, line staff relationships, accounting,: techniques, characteristics of the budgetees and of firm etc. A number of inputs into a budget system are related to the outputs of relevance, attitude and job satisfaction." [14] This definition discusses all the aspects of budget and the process of budgeting. It touches upon the factors like inputs, outputs, quality, quantity, participation, accounting methods and the psychological aspects of the factors involved in the process.

Budgetary control system is powerful tool to analyse the instability and unpredictability in the business environment. To forecast the possibilities and probable speculations budgetary control system is necessary. To reassert this, Nicolas Berland (2001) in his *scholarly and novel research paper titled, "Environmental Turbulence and the Functions of Budgetary Control" chronicles, "Budgetary control is a potentially significant tool when the economic environment is unstable and unpredictable; the analysis of its development demonstrates that its use has dramatically expanded since the time when companies have been able to run forecasts. In order to help them develop budgetary control, companies have implemented strategies that have reduced risks and hence improved their ability to make accurate forecasts."* [15]

Budgetary control system amalgamates all departments and departmental activities in terms controlling monetary values. Also it covers planning, coordinating, motivating and controlling. In *Extending the Boundaries of Management Accounting Research* (2001) Otley, the author, enunciates, "budgetary control as consisting of planning, controlling, co-coordinating and motivation through money values and departments within an organisation from an overall company control perspective, more recently notes that the assumption of budgetary control is that it is the main integrative control method for most business enterprises. The assumption being that an organization's business plan can be represented financially by the budget and that the budget can be used as a monitoring and controlling method for the complex issues of the business plan. This emphasis sees the budget linked to the overall attainment of organisation performance targets." [16] Here, Otley insists upon the managerial skill at the apex of monitory activity. According to him, for the external public, a budget is the financial plan but internally, it is a more complex activity being monitored and controlled by the management. It is a mechanism of management performance which not only assesses the performance of the company but also the models of customer relationship.

However, budgetary control system can be achieved through enforcement of internal controls in the form of internal audits; internal checks within functions and activities; administrative controls in terms of ensuring effective personnel policies, operational rules, regulation, procedures and methods; segregation of duties into initiation, approval, authorizations, execution and recording of transactions; chart of accounts which indicate cost items, cost centers, cost levels and expenditure boundaries; maintenance of proper books of accounts which are books of prime entry, cash book, journals and ledgers; issuing accounting instructions in respect of purchase, stock and receipts, periodic stock-taking and imprest retirement and reimbursements; and issue of accounting manuals and adoption of accounting policies in respect of assets disposals and depreciation.

For managers and administrators, budgetary control system provides a guideline in planning and forecasting an activity. Daniel Badu (2011) in his treatise titled, *An Investigation of Budgeting and Budgetary Control at Ernest Chemist* vocalizes, "Budgetary Control system provides guidelines for managers and supervisors to ensure that they think well ahead of time to foster effective utilization of limited resources of the organization…The preparation of budget helps in designing or clarifying the lines of horizontal or vertical communication within the organization." [17] In designing the policies and work accordingly the managers need budgetary control system. Accordingly, it also involves comparison of actual levels of performance against budgets and reports all variances with proper analysis to provide a basis for future courses of action. Further, it is an overall strategy of the management regarding the use of resources. Similarly, budgetary management is one of the processes of the organisation. Budgetary management remains at the centre of all other processes like, production, sales, purchase and quality control. Further, it helps the management to make the overall strategies of the organisation. It involves the continuous comparison of actual performance against the budget to ensure whether the plan is achieved or to provide a basis for its revision. This, further, prepares the right path and helps in avoiding the deviation.

Correspondingly, transparency and accountability in budget process are the indicators of participatory and healthy budget which is achieved by the organisations with democratic corporate environment. Josh Lerner and Jez Hall (2007) in their research article titled, "More Transparency, Better Decisions" state, **"**One reason why participatory budgeting works so well is its transparency. The decision-making process is open and visible to all. Participants base their budget decisions on predetermined and publicly disclosed criteria. Public meetings and information sharing also require government and community decision-makers to account for their actions. They build greater trust and confidence in spending decisions, and in government itself. Democracy is time-consuming. Participatory budgeting, however, can make democratic decision-making more efficient and effective. It increases budgeting outputs, so that they include not only funds allocated, but also resident education and empowerment, better local intelligence, the development of new community organizations, and the inclusion of marginalized people." [18] This definition configures the voice of all that participate in the process of budget. It also traces the margins as they have democratic atmosphere in decision making and spending. As a result, the quality of projects improves when they are based on the knowledge of the people who actually work and can understand the problem they confront. The preferences and decisions are reflected in the local needs. Participatory budgeting has even helped attract new funding.

Thus, the concepts budget, budgeting and budgetary control have undergone a tremendous modification from time to time in Accountancy and Costing. With scientific and technological advancements in the arena of these subjects, the concepts have become more sharp, pointed and micro based. The crudeness and fuzziness has disappeared in the modern and post Globalization era making a sharp distinction in every possible aspect related to these concepts. This, of course, facilitates scholars, researchers, managers, writers and students to study and understand the subject in depth. The study is a suggestive of a future possibility to have a novel aspect or approach to the said concepts.

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