CPD Seminar

Budgeting & Budgetary Control Techniques

Best Practice Presentation

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• Budgeting defined
• Why do business Executives hate the budgeting process?
• Budgeting and budgetary control process overview
  ✓ Reviewing & confirming corporate strategy
  ✓ Creation of the annual budget
  ✓ Approval of the annual budget
  ✓ Monitoring & control actual results to budget
• What are the hindrances to an effective budgeting process?
Definition/meaning
Budgeting Defined

A process, not an event.

• It is a systematic process for:
  ✓ Expressing future plans in formal quantitative terms.
  ✓ Allocating resources to achieve strategic goals.
  ✓ Monitoring progress toward goals.
  ✓ Controlling spending.
  ✓ Predicting cash flow and profits.
  ✓ Communicating plans in an orderly manner throughout the organisation.
Big Problem!
Why Do Business Executives Hate Budgeting?

They say:

• It is divorced from the objectives they are held accountable for.
• Their numbers disappear from the final outcome.
• It is fixed against a changing environment.
• It is cumbersome and takes long to complete.
• It is outdated before it is completed.
• It involves too many iterations.
• It involves too many people.
• There is too much game play.
• It includes allocations that they cannot control.
• It does not help them run their businesses.
Budgeting & Budgetary Control Process Overview

1. Review & Confirm Corporate Strategy
2. Create Annual Budget
3. Approve Annual Budget
4. Monitor & Control Actual Results to Budget

The process flows as follows:
- Review & Confirm Corporate Strategy
- Create Annual Budget
- Approve Annual Budget
- Monitor & Control Actual Results to Budget

This cycle is repeated to ensure ongoing budgeting and control.
Defining The Relationship Between Budget & Strategy

- Clearly define the strategic goals before budgeting begins
- Establish and foster formal and informal channels of communication
- Communicate goals and strategies to all budget developers
- Ensure appropriate procedures & systems are in place so that information is uniformly reported & easily accessible
- Provide training for budget developers so that they recognize how strategy affects budgeting
Strategic Alignment Of Budget To Strategy: Best Practice & Controls

- Link budget development to the corporate strategy.
- Ensure capital & operating budgets horizons are consistent with strategic goals.
- Submit capital & operating budgets simultaneously & integrate them in terms of goals & purpose.
- Identify risks in budgeting & develop strategies to manage them.
- Foster communication to develop & strengthen strategy.
- Train budget developers in linking the budget to the strategy.
- Use performance measures to mark progress toward goals.
• Number of budgets produced annually.
• Number of ad hoc budgets created to special needs.
• Number of full-time equivalent staff as a percentage of total staff devoted to budgeting.
• Total cost of financial budgeting and planning as a percentage of revenue.
Budgeting & Budgetary Control Process Overview

Develop/Review & Confirm Corporate Strategy → Create Annual Budget
Budget Process Road Map

- Gather internal & external information.
- Verify the data sources to ensure completeness and accuracy.
- Create assumptions and estimates.
- Create the sales budget.
- Create the production budget.
Conditions Necessary For Annual Budget Creation: Best Practices & Controls.

- Develop budget collaboratively, involving all stakeholders.
- Document & communicate policies & procedures; ensure all stakeholders understand their roles.
- Understand users of the budget.
- Provide training to those involved in the budget process.

- Link cost management efforts to the budgeting.
- Conduct companywide meetings to establish budget timelines & responsibilities.
- Designate a budget manager to coordinate the process.
- Use adequate hardware & software to support the budgeting process.
- Avoid re-keying data and use templates to reduce errors.
- Develop budgets that are flexible for changing conditions.

- Ensure the integrity of systems, databases & records.
- Ensure data is available electronically to budget users.
- Make managers understand that they are responsible & accountable for their department budgets.
Conditions Necessary For Annual Budget Creation: Performance Measures.

• Number of budgets produced annually.
• Number of ad hoc budgets created for special needs.
• Number of budget revisions.
• Number of errors in assumptions.
• Results of customer satisfaction surveys.
• Number of employee suggestions for process improvements.
• Employee satisfaction scores.
• Budget creation cycle time.
Budgeting & Budgetary Control Process Overview

- Develop/Review & Confirm Corporate Strategy
- Create Annual Budget
- Approve Annual Budget
Annual Budget Approval Components

- Define the timelines for budget approvals.
- Submit the preliminary budget for approval.
- Modify the budgets and incorporate changes.
- Approve the budget.
- Distribute the approved budget to departmental managers.
How to Ensure Stakeholder Buy-in In The Approval Process

• Best practices & controls
  • Establish a written approval process involving critical users of the budget.
  • Reduce budget complexity & cycle time.
  • Establish reasonable timelines for approving capital & operating budgets.
  • Use cross-functional teams & consistent review procedures to evaluate budgets.
  • Create accountability for untimely budget approvals.

• Performance measures
  • Average length of time to create and approve the budget.
Budgeting & Budgetary Control Process Overview

1. Develop/Review & Confirm Corporate Strategy
2. Create Annual Budget
3. Approve Annual Budget
4. Monitor Actual Results to Budget
Compare Actuals To Budget: Implement, Monitor & Control

1. Upload the approved budget into the ERP system.
2. Capture the actual results.
3. Compare the results to the budgeted amounts.
4. Identify & investigate significant variances.
5. Establish & implement corrective actions.
• Ensure that budgets are at the same level of detail as the actual results.
• Provide managers with the decision-making authority to influence the measures on which they are evaluated.
• Evaluate performance based on controllable factors.
• Set specific performance measures for departments & business units.
• Conduct monthly actual-to-budget reviews & investigate all significant variances.
• Monitor performance measures over time against desired performance levels.
• Establish accountability for improving performance and incorporate it into the process owner’s evaluation & compensation.
Conditions Necessary For Effective Budget Evaluation: Performance Measures

- Variance of actual-to-budget items as a percentage of budget.
- Percentage of discretionary spending occurring in the last financial quarter.
- Ratio of cost savings to total costs for cost management efforts.
- Ratio of expected return to actual return on capital proposals.
- Ratio of failed to successful capital proposals.
Budget Process Flow: A Typical Example

Company / Business
- Communicate detailed instructions as to the content of the Budget

Consolidation Group
- Budget Preparation (Department Level)
- Approve Budget
- Yes
- No
- Budget Preparation (Segment Level)
- Monitor actual results to budget
- Review & confirm corporate strategy

Department
- Budget Preparation (Plant/Section level)
- Yes
- No
- Approval

Segment/Plant (Section)
- Budget Preparation (Plant/Section level)
- Yes
- No
- Approval

Board
- Communicate Approved Budget
- Yes
- No
- Upload approved budget into ERP

Approval
- Approve Budget
- Yes
- No

Communicate detailed Instructions as to the content of the Budget

Review/confirm strategy
- Create Budget
- Approve Budget
- Monitor actual to budget
Hindrances
Key Issues That Hinder An Effective Budgeting Process

Best practices & controls
• Performance measures are not aligned with company objectives.
• Performance measures are inaccurate.
• Performance measures are unknown.
• There are too many performance measures.
• Performance measures are not quantifiable.
• Performance measures are ignored.

Other key concerns
• Managers frequently request expenditures in excess of budget.
• Actual results differ largely from the budget (i.e. Unadjusted forecasts have been closer to the actual results than the approved budget).
• Monitoring is not performed continuously throughout the year.
Thank You