Essay on fiscal accountability

Business, Company

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Introduction

Financial budgets refer to monetary estimates of expenditure that the organization expects to incur in future as it carries out its periodic business operations.

Budgets have proven to be important business tools over the course of time. One of the most important uses of the budget is that it can be used by the management of a business entity to make decisions. Decision making is the most important process in a business entity because it determines the direction of the business after a financial period. Financial periods are marked by losses or profits depending on how the entity has performed in comparison to the previous financial periods. In addition, the firm's revenue may have remained constant as a result few changes in the macroeconomic environment.

After analyzing the performance of the firm in during a certain financial year, the firm must plan ahead on how it will carry on and finance its future operations. Business entities are always considered to be a going concern. This is an accounting policy where they are presumed to continue trading

into the foreseeable future. In order to implement this principle correctly, they need to budget and present these financial plans to the management who then make decision.

How Managers Use Budgets to Make Decisions

First of all, managers make decisions using budgets by getting involved in the process of budget development. The budget will have a stern effect only if people who have authority within the business take part in its formulation. This is because the managers have the ability to control the finances of the firm. The other employees deal with the daily operations of the firm. As a result, they are better placed to anticipate what the firm needs in the future. The anticipation forms a basis of the future cost analysis which determines how much money the firm is going to spend for trading in the next financial year. As a result, managers can then decide on the most appropriate sources of capital.

The managers can decide to borrow funds, retain a portion of the profits generated or issues out the stock of the business entity in the financial markets. Managers can therefore use budgets to determine the optimal mix of capital to be used by the business. The mix should generate the highest possible revenue for the firm while ensuring that it incurs the least possible cost. This is called capital budgeting. It helps manager to make the capital decisions.

Managers can also use budgets to make decisions related to the firm's creditors. This is made possible by the Cash Flow budget plan. This plan combines the capital expenditures of the entity with income statement to determine the ability of the business to meet its financial obligations as and

when they fall due. This determines the credit worthiness of the firm as it shows how much its assets can be offset against its liabilities. The cash flow budget is important to managers because it describes the level of liquidity of the firm. Liquidity is the rate at which the tangible and the intangible assets of the firm can be converted into cash.

According to Maher, Stickney and Weil, managers have the ability to make decisions on the nature of the firm's credit policy by using the Cash Flow Budget. The credit policy as decided by the manager is important to determine the credit period within which the entity has the ability to generate adequate returns to service its debts.

Managers can also use the budget to establish and design the marketing strategies. The revenue and estimate sales can be derived from the Income Expense Budget. This budget contains all the expenses to be incurred as the firm markets and sells its products to its consumers. Managers are involved in the marketing through their decisions on the marketing strategies adopted by the firm. Aggressive marketing strategies like prolonged advertising require heavy allocation of funds to the marketing department. The firm can adopt such policies to reach as many clients as possible and maximize its sales.

In their analysis of management versus financing, Maher, Stickney and Weil argue that recognizing uncertainty in business is the key towards good budgeting. The method advocates for the use of the accruals concept which addresses uncertainty and reduces the level of subjectivity when making financial plans.

The uncertainty in business can be assessed using simulations. In

management accounting, it may be easy to find an analytical solution of one variable, for instance, sales (Maher, Stickney & Weil, 2001, 4). The most likely instance of the variable can be found using the Triangular distribution formula. In this method, it is easy to determine the value of sales at their best, worst and when they are at an optimal level (average). However, when other variable come into play, for example, cost and consumer behavior, it becomes difficult to make the correct sales estimates. Budgets help managers to make accurate decisions by plotting estimates around these values.

Conclusion

Decision making is a primary responsibility of business managers. Budget estimates cover the entire departments of the business which makes it possible to estimate the future costs and anticipated revenue for the coming year. They are an important decision making tool.

References

Maher, M., Stickney, C. P., & Weil, R. L. (2001). Solutions manual, managerial accounting: An introduction to concepts, methods and uses. Fort Worth, Tex: Harcourt College Publishers.