

Advantages and disadvantages of involving managers in budgeting report samples

[Business](#), [Company](#)



Introduction

A budget is a systematic way of allocating human, physical and financial resources so as to achieve the strategic goals of a business or an organization. Budgets help businesses to monitor their progress towards the set goals and objectives. The practice of involving the managers in budget making rather than simply imposing budget on them is called participatory budgeting. The main reason behind involving the managers in the budget making process is to assign responsibility to subordinate managers and place some form of personal ownership on the final budget. Over the last two decades, management accounting research has resulted in ambivalent findings on the effects and consequences of participatory budgeting. The report below shall summarize articles in a bid to identify what different persons have to say about participatory budgeting and its advantages and disadvantages.

Arthur Andersen (2000). Best Practices: Developing Budgets, Budgeting Article | Inc. com. Retrieved December 12, 2013, from <http://www.inc.com/articles/2000/01/16379.html>

Arthur Andersen studied the some leading companies that are best performers in budget development process. Arthur finds that it is important to improve the budget process for a better performance of any business. He states that effective budgeting will enable a business to move more effectively and efficiently towards its goals, objectives, and mission as well as compete effectively in the highly competitive business world.

He states that involving managers in budget formulation is important due to:

- It helps in communicating strategic goals since it improves communication in the organization.
- It enables a business to tie performance measures other than meeting budget targets.
- It allows the business to link cost management to budgeting and this is of utter importance in the variance analysis that shall be performed at later dates.
- It will enable a business to develop budgets that accommodate change.

However, he finds that the practice has its drawbacks too.

- Some managers are not proficient in budgeting and if involved in the budgeting process, their contribution might be vague and misleading which will lead to misappropriation of resources.
- Managers' personal interests might prevail and this will have a negative effect on the business.

M. W. Waldron, J. Vsanthakumar, and S. Arulraj (2010). Chapter 13 -

Improving the organization and management of extension. Retrieved from <http://www.fao.org/docrep/w5830e/w5830e0f.htm>

The management functions include expense control, fiscal planning, accounting and revenues. Waldron et al. clearly notes that budgeting requires specific planning and a thorough considerate of intentions of the company as well as future programs, ability to predict the unpredictable future and a sense of economic conditions and realities. Effective

participation of managers in the budgeting process enables a formulation of

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a budget that will be:

- Acceptable to the managers as they will feel part and parcel of it.
- This will further make it easy for them to internalize its contents.
- Possibility of formulating a realistic budget is high due to the involvement of managers since they are the ones with a deep knowledge of the real abilities and constraints of the business.
- It enables the management to agree on the most rational use of its resources.

However, involving managers may not always be good due to:

- Budgetary slack may arise
- It may result to negative motivation
- It may hamper the effectiveness and efficiency of the entire budgeting process.

McClamroch, J. Jacqueline J. and Steven L. (2001). " Strategic Planning: Politics, Leadership, and Learning." *The Journal of Academic Librarianship* 27, no. 5 (September 2001): 372-378.

The journal investigated the challenges brought about by the shrinking budgets in high education and the growing demand for services and resources. It states that organizations must confront the realities of new time, practice strategic allocation of resources and focus their energies on budgeting. Strategic planning is must incorporate budgeting and it is a necessary activity for organizations to pursue.

It states that involving managers in the budget formulation process helps an organization to develop associated budgets, competitive allocation and

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determine the politics of the business as well as increase the transferal of information.

Participatory budgeting may bring about the following disadvantage: May result to unrealistic budgets especially underestimates since managers will always try to propose low budgets since large budgets may not be attainable and this might make them lose their jobs. They therefore want to ensure that they have a job security.

Stephen C. and David T. (2003). Practice Developments in Budgeting: An Overview and Research Perspective. Journal Of Management Accounting Research, Volume Fifteen 2003 pp. 95–116.

In nearly all organizations, budgeting is the cornerstone of the management control process. However, practitioners argue over the traditional imposed budget and the modern participatory budget. The two budgeting techniques determine how effective the organization will achieve its goals and objectives as well as the general performance and efficiency of the organization.

Participatory budgeting is presented as being advantageous in the following ways:

- It makes the budget process more responsive to priorities
- It makes management practices more flexible
- Creates financial discipline
- It will enable the management to identify and implement the best control system hence any estimates variation that might occur in the course of business operations might be rectified with immediate effect.
- Managers will assist in setting and implementing the required standards of

efficiency.

- Leads to an increased level of efficiency

It is however limited by the following drawbacks:

- The benefits of the participation might be limited by the personality traits of the budgeters

- Participation may encourage managers to adopt a self-centered approach.

They will therefore concentrate majorly on maximizing their own benefits rather than engage on maximizing the reimbursements of the entire organization.

Souza, C. (2001). Participatory budgeting in Brazilian cities: limits and possibilities in building democratic institutions. *Environment and Urbanization*. doi: 10. 1630/095624701101285540

The journal investigates how effective participatory is in the development of cities in Brazil. It outlines the benefits of participatory budgeting as:

- It is costly to involve the managers in the budgeting process since it means that more people will be involved in the budgeting process and this will have some associated increase in expenses.

- It facilitates the identification of difficulties that might be faced in the introduction of a cost control system.

- It enables the business to take into account other minor factors that might be hampering the managers' performance at a personal level.

However, its drawbacks include:

- Managers not being proficient enough in budgeting

- Personal interests might prevail during budgeting

- It is costly and less efficient since there is lengthy consultation

Epstein, M. J., & Lee, J. Y. (2010). Advances in management accounting and budget setting: Volume 18. Bingley: Emerald

The benefits of involving a manager in budget setting is that he or she may be able to come up with critical decisive decision making in the subject of interest in running of the company. Moreover, the manager may lead to discovery of particular perspective in selected items that are essential in the budget. When the committee sets up a budget, there is greater possibility that the general outline may be biased. However, when a manager is included in the setting of the budget, the chance of biasness may be reduced due to the manager's different perspective on the same issue of interest.

The manager may have the ability to determine the cuts and their impacts to the company in a specified department of common interest. This clearly demonstrates the significance of involving a manager when making decisive decisions in a company concerning the budget.

Epstein, M. J., & Lee, J. Y. (2010). Advances in management accounting and budget setting: Volume 18. Bingley: Emerald.

Operational managers has the ability of providing a more detailed picture of what the company needs in the present moment and in the predicted markets. In this argument, the managers can be described as a figure in the company who has an ability to figure the exact amount of resources within the company. In this regard, the expenditure of the company would be determined hence drawing a perfect budget for the company. However, different operational managers from various departments in a company would mean that set up of the budget would not be effective due to singular

perspectives. When managers are involved in budget setting, it would imply that the number of advisory members would be higher than normal hence interconnection of unorganized ideas on the estimated amount needed by the company to create a perfect and reliable budget.

Moreover, when operational managers are involved in the committee when setting up the budget, it may imply that the sense of global concern for the company would not be there. The managers are always egocentric and do fight for their salary increment at the expense of the company's interest. In most cases, managers may only focus on justification for the value of the budget rather the future outcome of the same. They do not give priorities to the most important expenditures that can withstand long-term market waves.

Jensen, M. (2001). Corporate Budgeting Is Broken—Let's Fix It. Harvard Business and Budget Setting Review, 2, 8. Retrieved from <http://hbr.org/2001/11/corporate-budgeting-is-broken-lets-fix-it/ar/1>

The inclusion of manager's opinions when setting up a budget may pose a risk to the company due to difference in individual's perspective. The managers expect that their opinions and suggestions would have a positive impact in the company; hence they do not expect their opinions to be considered as unimportant. In order to prevent their pride and interest, their suggestions are employed when the budget is being set up hence biasness. However, if the company's operational managers are not involved in the process of setting up the budget, the moral and financial level of the company may be negatively affected.

Alan S Dunk, Alan Kilgore (2003), TOP MANAGEMENT INVOLVEMENT IN R&D

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BUDGET SETTING: THE IMPORTANCE OF FINANCIAL FACTORS, BUDGET TARGETS, AND R&D PERFORMANCE EVALUATION, in (ed.) 11 (Advances in Management Accounting, Volume 11), Emerald Group Publishing Limited, pp. 191-206

According to the document "Top Management Involvement in R & D Budget Setting", the authors Alan Dunk and Alan Kilgore discuss the increase/decrease in organization's top management security measures when a manager is included or excluded when setting up a budget setting for an organization. In this document, Research and development sector is keenly observed in providing the concept behind inclusion of managers when setting up a budget. The document explains the implication that comes as a result of managers getting involved in R&D budget setting. The second explained significance of manager's involvement in budget setting is the critical evaluation that managers make before the budget is approved for the involved organization. In presence of a manager in a budget setting, quality assurance is guaranteed for the committee and the organization in general. The level of managerial assumptions is extremely high and hence inaccuracy that could lead to drawbacks in a company intensively overrules the budget. In this regard, it openly means that the chances for an economic downturn in the company are extremely high. This happens as a result of higher rate of spending in a budget. Moreover, involving managers in budget setting increases the chance of making rigid decisions which could formulate a budget that may pose a threat in company.

Riley, J. (2012). Budgeting - Limitations of Budgets. Finance and accounting in relation to budget setting. Retrieved from <http://www.tutor2u.com>

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net/business/accounts/budget_limitations. html

The time required when constructing a budget is extremely too much for people in a managerial position to bear. This time consumed by the managers to set up a budget could be used somewhere else for the purpose of progressively steer forward the company. The work involve is extensively tedious and thus could lead to poor judgment on the decision or suggestions made in the budget from the managers.

When a more experienced manager is involved in setting up a budget, he may introduce complex budgetary system that may interfere with the employees of the company. Therefore, in order to prevent the effects of this, managers should not be included when setting up a budget for any company. The manager may intentionally increase the revenue and the expenses.

References

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