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# Activity Based Budgeting in Organizations

Have you ever wondered what exactly is up with Budgeting? This informative report can give you an insight into everything you've ever wanted to know about Budgeting.

Activity based budgeting is not new. As early as 1990, some organizations in countries like the USA and Australia implemented this new budgeting program to replace the old and known method of budgeting, the "line item budgeting."

Activity based budgeting is a method of budgeting in which activities that incur

costs in each function of an organization are established and relationships are defined between activities. This information is then used to decide how much resource should be allocated to each activity.

In other words, activity based budgeting is budgeting, planning and controlling by activities rather than cost elements of an organization. For users of this budgeting program, they claim that it engages everyone in thinking about how they can better create value for organization. It develops a flexible budget based on activity work load that is not as rigid as ledger of the line item budgeting that pre-identifies costs eventhough that cost may not be of use at all.

Activity-based budgeting is simply organized common sense. More specifically, activity based budgeting is a technique for enhancing the accuracy of financial forecasts and increasing management understanding. When automated, activity based budgeting can rapidly and accurately produce financial plans and models based on varying levels of volume assumptions.

Activity based budgeting also can eliminate much of the tedious work in traditional budgeting. Activity based budgeting analyzes the products or services to be produced, what activities are required to produce those products or services, and what resources need to be budgeted to perform those activities. Simply put, activity based budgeting is the reverse of the activity-based costing process to produce financial plans and budgets.

With the advent of powerful and low-cost database systems, activity based budgeting is allowing businesses to reduce costs, better utilize resources, and achieve strategic objectives.

The Australian National Audit Office has identified the advantages of activity based budgeting:

See how much you can learn about Budgeting when you take a little time to read a well-researched article? Don't miss out on the rest of this great information.

#### The Advantages

- Output costs are supported by a schedule of costed activities
- Opportunities to examine work processes
- Identifies non value-adding activities that can be eliminated
- Basis of a performance measurement system and direct link between strategic

goals and operational realities

- Enables cost profiles to be managed
- Accurate costing data for operational management
- Costs are transparent, understandable and actionable

#### Disadvantages

- Activity definition may become too detailed and the model may become too complex and difficult to maintain
- Underestimation of the task of collecting activity driver data
- Implementation may be considered a financial management ?fad? and there is insufficient commitment from operational managers

## Activity Based Budgeting Disadvantages

- Usually requires buying Activity Based Budgeting software
- Requires training of all managers including budgeting department
- Requires people to really understand what drives their budget
- Eliminates excuse that activity volume changed because it makes visible volume changes
- Requires everyone to collect or estimate activity volume

By understanding how resources are transformed into products or services, and by focusing on the cost of activities, activity based budgeting helps an organisation to obtain a greater understanding of how costs behave in their organization and which activities create significant amounts of cost. Organizations can then begin to control their costs based on tangible activities rather than relatively uninformative general ledger or cost center reports.

### About the Author

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