BUDGETING AND BUDGETARY CONTROL PRACTICES AND PROCEDURES IN TIMBER FIRMS WITHIN KUMASI METROPOLIS

Evans Frimpong-Manso

College of Distance Education, University of Cape Coast, Cape Coast, Ghana

ABSTRACT

The purpose of this study was to examine the budgeting and budgetary control practices and procedures in the timber firms in the Kumasi Metropolis. Specifically, the study examined the budgeting practices and approaches that exist in the timber firms, the importance of budgeting and budgetary control system as a performance measures at the timber firms, and the challenges that exist in the timber firms in Kumasi during the process of budget preparation and implementation. To tackle these objectives, opinions were elicited from all the 35 heads of departments and 53 deputies in four selected timber firms in the Kumasi Metropolis using census method. Questionnaire and interview guide were the main instruments used in eliciting data from the respondents. Frequency and percentage were used to analyse the quantitative data.

Results of the study showed budgeting and budgeting control measures are an integral part of timber firms. It serves as a basis of planning, controlling cost of operations and evaluating performance of workers of these firms. Despite the laudable benefits of budgeting, its preparation, implementation and execution need to be controlled and monitored to avoid deviations from the plan and serve as a basis for revising the budget put in place. Challenge of preparation, implementation and human factors that also tend to affect budgeting. Therefore, management should ensure that in the preparation of the budgets, serious thought would be given to the external environment, emerging technologies, organisational structure and size as well as culture of the organisation and the setting where the timber firms operate.

Key words: Budgeting; Budgetary control system; Budgeting practices; Budget preparation.

1.1 INTRODUCTION

Budgets are management tool that puts executives in control of the financial health of their company. It is an objective measures of the financial structure of a company’s operation and a tool that forces management to be accountable in a structured and objective way. Budgets as management tools by themselves are neither good nor bad. How managers administer budgets is the key to their value. Budgets as plans are pointless unless there is a periodic check on what is being achieved. Problems can arise at any point during the implementation of a plan. Unless a specific check is made during the implementation of plans, they can go unnoticed for so long that they will be impossible to remedy (Abernethy & Brownell, 1999). Control measures should therefore be carefully planned so that they spotlight the problems that are likely to arise out of implementation of plans.

1.2 PROBLEM STATEMENT

Pierce (2004) stated that limited resources call for the need to plan and exercise control over their use and that budget are the most effective way of corporate planning and control. Budgeting serves as a tool to guide management to ensure proper use of resources. Quite apart from these advantages budgeting and budgetary control practices and procedures have on firms, there has been no substantive study on the issue among timber firms in the Kumasi Metropolis (Ghana Forestry Commission [GFC], 2010). Therefore, the aim of this study is to evaluate budgeting and budgetary control practices and procedures in the timber industry to access the effectiveness of budgeting decisions in controlling operational cost.

Further motivation for the study is the lack of research involving survey of budgeting and budgetary control practices among timber firms in the
developing countries. From the literature, it is realised that a lot of such studies have been conducted in most of the advanced countries such as United States of America, United Kingdom and Australia (Horngren, Datar, Foster, Rajan & Ittner, 2009). However, research on the effectiveness of budgeting and budgetary control practices in developing countries of which Ghana is no exception is lacking.

1.3 RATIONALE OF THE STUDY

The purpose of this study was to examine the budgeting and budgetary control practices and procedures in the timber firms in the Kumasi Metropolis.

1.4 RESEARCH QUESTIONS

The objectives were used to formulate specific research questions to guide and provide direction to the study. The research questions formulated were:

1. What budgeting practices and approaches exist in the timber firms in Kumasi?
2. What are the importance of budgeting and budgetary control system as a performance measures at the timber firms in Kumasi?
3. What challenges exist in the timber firms in Kumasi during the process of budget preparation and implementation?

1.5 SIGNIFICANCE OF THE STUDY

Since budgeting serves as a control device and as means of appraising employees performance in most organisations, failure to examine the budgeting process and investigate into the causes of budgeting variances, turns to affect the overall management control system of an organisation, hence the need for this study. The study has a practical significance, as it is expected to uncover the causes of budget variances in the timber firms in Kumasi that hampers management’s efforts in promoting efficiency in its operations. It is also expected that the study will be beneficial to the management of these firms as the recommendations of the study will help management to improve upon its performance if they are implemented. Lastly, it is expected that the findings of the study will add to the available literature on the subject which will be beneficial to other researchers carrying out a study on the topic.

2.1 REVIEW OF RELATED LITERATURE

Budgeting and budgetary control is a fundamental and necessary tool in the management and administration of every organisation, irrespective of size, corporate objectives and form of ownership. It is an integral part of short-range planning and control in most organisations (Wood & Sander, 1998). Budgets as financial plans that set out anticipated revenues and estimated expenditures over a certain period of time have long been in use. Since their inception in the 1920’s, every serious company has made them the central part of their planning and control system (Drury, 2004). Their ability to co-ordinate the allocation of resources through internal communication while at the same time serving as a means of expenditure authorisation and evaluation base has made them the most important tool that is at the managers’ disposal today when running a company. It is exactly this importance that has contributed to budgets’ longevity and caused them to remain relatively unchanged in their use since the first days of their existence, especially the top-to-bottom approach (Drury, 2004).

Timber firms use management accounting techniques to assess their operations. The techniques include budgeting, variance and breakeven analyses. These management accounting techniques help organisations to plan, direct and control their operational activities, so as to achieve the objective of cost minimisation and thereby maximise profit. As organisations employ variety of procedures such as planning and budgetary policies, operating guidelines are put in place in order to facilitate the control of operations. Wood and Sander (1998) argued that in preparing budgets, one has to consider sales demand since production is geared towards the quantity of products demanded. Therefore, the system of controls and the resulting management style within an organisation can be either an important inhibitor or facilitator of a firm’s strategic initiatives (Anthony & Govindarajan, 2003).

Budgeting promotes planning and controlling of the activities of organisations. According to Hope and Fraser (2000), all organisations regardless of the type or size, need to develop a plan. They asserted that planning is one of the most important functions of management. It is therefore, a necessary requirement for management control. As organisations grow in size, budgeting becomes more critical. Large organisations cannot
relate on a couple of managers to plan for the entire organisation. Neither can large organisations expect effective planning to occur simply by casual face-to-face discussions among employees. Instead, large organisations, government organisations and non-profit making organisations must formalise the planning process. The formalisation and the detailed planning process can be classified as budgeting. Gyasi (2005) viewed budgeting as the process of preparing an organisation’s plan of action for a future period. This means that the organisation tries to come out with what it intends to do in the nearest future. Gyasi further asserted that it is always appropriate for firms to prepare yearly or semi budget within an organisation.

Once adopted, a budget becomes an important basis for evaluating performance. Thus, it promotes efficiency and serves as a deterrent to waste and inefficiency (Weygandt, Kieso & Kell, 2008). The success of the budget process depends on managers’ success in setting appropriate targets for which they are held accountable. Just because a plan is set down on paper does not mean the plan will carry itself out. Control is exercised via the budget hence the name budgetary control. Blumentritt (2009) is of the view that organisations need to integrate strategic management and budgeting. Organisations and institutions use budgeting and budgetary control procedures to enable them translate the firm’s strategic plans into day-to-day activities which enable them efficiently and effectively achieve their goals.

The production and export of timber and timber products serve as one of the very important fulcrum around which the economy of Ghana thrives, contributing six percent to Ghana’s Gross Domestic Product, hence, higher performance of the firms in the timber industry is crucial for the achievement of macroeconomic stability for Ghana as a country (GFC, 2010). The success or not of the timber industry depends greatly on the ability of timber companies in Ghana to manage resources both natural and human effectively and efficiently in their operations. Timber Industries in Ghana have scarce raw materials to use in their operations. As a result of over reliance and misuse of natural resources by firms in the timber industry, they have contributed to the depletion of vegetation in Ghana leading to environmental degradation (GFC, 2010).

Pierce (2004) stated that limited resources call for the need to plan and exercise control over their use and that budget are the most effective way of corporate planning and control. Control measures should therefore be carefully planned so that they spot-light the problems which are likely to arise out of implementation of plans. Budgeting and budgetary control serves as one of management tools for effective planning and control to ensure proper and efficient use of economic resources in Timber firms.

A survey conducted by Chow, Cooper and Waller (1988) revealed that an increase in the use of budgets by Singaporean companies when 97 percent out of 109 companies surveyed reported high use of budgets. Harper (2000) also posits that budgeting promotes co-ordination and communication in an organisation. Harper further asserted that budgeting provides basis for planning, performance appraisal, motivates employees, improves the allocation of scarce resources and economise management time. In 2001, Joshi surveyed 60 large and medium size firms. All (100%) the respondents indicated that they used budgets for planning day-to-day operations and cash flows, 93 percent said that they used budgets for controlling costs and 91 percent reported that they used budgets for planning financial position. Joshi’s (2001) study also revealed that Indian firms perceived budgeting to be one of the more important management accounting tools in the future. Lastly, Joshi (2001) study revealed that Indian companies were using strategic formal planning and long range forecasting techniques in budget planning.

In Singapore, for example, about 95 percent of the 174 companies surveyed used budgets as a financial control tool (Chong & Chong, 2002). Horngreen, Foster and Datar (2000) reported in their study that because of future uncertainties assumed conditions may not necessitate the revision of budgeted targets. Lack of resources and lower morale are always linked to production in organisations because due to economic theory of scarcity in relation to demand and satisfaction, there is always gaps left in achieving fully what organisations intend to achieve. Drury (2004) also avers that budgets are time consuming and costly to put together. Furthermore, Lucey (2004) contended that budgetary control is a means to stay on focus and prevent deviation from the plan. Budgetary control enables management to work in line with the objectives and targets set for the organisation and avoid deviation from the original plan. Certain human factors such as personal interest and negative work attitudes can also cause problems that may affect budget decisions. Peirce (2004) indicated that
in order to avoid the human factor problems that affect budget decisions, good attitudes which are the key to successful budgeting need to be developed among employees, where management explain to its staff that budgets are the most effective way of corporate planning and control.

3.1 METHODOLOGY

Since the study entailed a survey of departmental heads and their deputies’ view on the issues, situations and processes; the descriptive survey design was deemed the most appropriate. There were only four timber firms in the selected area that conform to the criteria the study was interested in. The study focused on firms that were considered to be large in terms of size and coverage area. As the heads of the departments and their deputies are considered to be one of the major groups that contribute to the success of these timber firms, this research examined their views on the nature of budgeting and budgetary control practices and procedures in the firms. Currently, there are 35 heads of departments and 53 deputies in these four selected timber firms in the Kumasi Metropolis (GFC, 2010).

3.2 SAMPLE AND SAMPLING PROCEDURE

The study makes use of the census method to capture all the 35 heads of departments and the 53 deputies in the accessible population. The use of the census method was appropriate and feasible since the accessible population of the study was small. The census again was necessary since the elements were quite different from each other.

3.3 INSTRUMENTATION

The questionnaire and interview guide were the sole data collection instruments used in collecting the data. The questionnaire was made up of 52 items with seven sections: A, B, C, D, E, F, and G. Both close-ended and open-ended form questions were used for the items in the questionnaire. The interview guide on the other hand was made up of 16 items. The interview guide helped the researcher to probe into issues and to follow the order dictated by the situation in other to obtain appropriate data qualitatively for the purpose of triangulation. To enhance the validity of the research instruments, the structured questionnaire and the interview guide were made available to experts to review and comment on with the view of establishing content validity.

In finding the reliability of the questionnaire, it was pilot-tested in December, 2011, on a sample of 15 respondents made up of heads of departments and deputies in FABI timbers limited, within the Ashanti region of Ghana. FABI timber limited was selected because it operates in the same region in the Atwima Mponua District that share similar characteristics as those timber firms in the Kumasi metropolis which is the selected study area. The Cronbach’s alpha coefficient of the questionnaire calculated was 0.72 which according to Pallant (2001) is acceptable. The researcher administered the instruments personally. The researcher conducted the interview simultaneously with the questionnaire. Only fourteen out of the eighty eight respondents who answered the questionnaires were interviewed. The purpose of the interview was mainly for triangulation and confirmation of the data obtained from the questionnaire. The data collected were first grouped for editing to ensure accuracy and clarity. With the help of the Statistical Product and Service Solutions (SPSS) Version 16.0, frequency and percentage distributions were used to analyse the data.

4.1 RESULTS AND DISCUSSION

It must be noted that at the end of data collection, 88 heads and deputies of four timber firms in the Kumasi Metropolis were captured for the study. The results and discussions are presented as follow:

4.2 Research Question One

4.2.1 Budgeting practices and approaches of timber firms

The research question one was concerned with the views of heads of departments and deputies on the kind of budgeting practices and approaches that exist in timber firms. In relation to that respondents were asked to indicate the maximum duration of the budget their department prepares, key factors that they consider when preparing their budget and the budget approaches they use in their respective firms.
Most of the heads of departments and deputies of the various timber firms in the Kumasi Metropolis asserted that they prepare annual or semi-annual budget and one of the factors they consider most when preparing their departmental budget is sales demand. The views of the respondents confirm that of Gyasi (2005) who asserted that it is always appropriate to prepare yearly or semi-budget within an organisation. Also, Wood and Sander (1998) argued that in preparing budgets, one has to consider sales demand since production is geared towards the quantity of products demanded. There is therefore no need to produce quantities of products and keep them in store without finding market outlets for them. Production is done towards the quantities of products demanded. With respect to the type of approach used by heads and deputies of these firms, majority of them indicated that they use the top-to-bottom approach. Therefore this approach is considered to be the most existing approach in these firms. The most cited budget model was the fixed and/or incremental budget. The findings are consistent with the submission of Drury (2004) who reported that the approved budget is passed down from top management through the organisation to the appropriate responsibility centres and that the approved budget by the top management becomes the authority for the managers of each responsibility centre to carry out the plans contained in each budget.

4.3 Research Question Two

4.3.1 Importance of budgeting and budgetary control systems

Table 1: Reasons for budgetary control measures

<table>
<thead>
<tr>
<th>Necessary reasons in budgetary reporting system</th>
<th>Necessary</th>
<th>Not necessary</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Freq.</td>
<td>%</td>
<td>Freq.</td>
</tr>
<tr>
<td>As a basis of revising the budget put in place</td>
<td>88</td>
<td>100</td>
<td>0</td>
</tr>
<tr>
<td>To prevent deviations from plan</td>
<td>88</td>
<td>100</td>
<td>0</td>
</tr>
<tr>
<td>To find the causes of deviation from plan</td>
<td>85</td>
<td>96.6</td>
<td>3</td>
</tr>
<tr>
<td>To appraise the performance of managers</td>
<td>82</td>
<td>93.2</td>
<td>6</td>
</tr>
</tbody>
</table>

Source: Field data, 2012.

Though it was the least but it is significant enough to be considered as one of the important reasons for budgetary control. The findings corroborate with the submission of Lucey (2004) who contended that budgetary control is a means to stay on focus and prevent deviation from the plan.
Budgetary control enables management to work in line with the objectives and targets set for the organisation and avoid deviation from the original plan.

4.4 Research Question Three

4.4.1 Budget challenges

The study delved into the challenges of budgeting in an organisation. In this study, three categories of challenges were identified. These were challenges related to budget preparation, implementation and decision making which deals with human factors. The challenges confronting heads of departments and their deputies in budgeting preparation in timber firms are shown in Table 2.

Table 2: Challenges confronting respondents in budget preparation

<table>
<thead>
<tr>
<th>Challenges</th>
<th>Always</th>
<th>Sometimes</th>
<th>Never</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Freq.</td>
<td>%</td>
<td>Freq.</td>
</tr>
<tr>
<td>Poor forecasting</td>
<td>4</td>
<td>4.5</td>
<td>81</td>
</tr>
<tr>
<td>Lack of resources</td>
<td>0</td>
<td>0.0</td>
<td>88</td>
</tr>
<tr>
<td>Lower morale</td>
<td>0</td>
<td>0.0</td>
<td>88</td>
</tr>
<tr>
<td>Operational difficulties</td>
<td>0</td>
<td>0.0</td>
<td>87</td>
</tr>
<tr>
<td>Time consuming process</td>
<td>0</td>
<td>0.0</td>
<td>81</td>
</tr>
<tr>
<td>Difficulty to define objectives</td>
<td>0</td>
<td>0.0</td>
<td>56</td>
</tr>
</tbody>
</table>

Source: Field Data, 2012. (n = 88)

As presented in Table 2, only 4 (4.5%) respondents indicated that they were always faced with poor forecasting challenges. More than 90 percent of the heads and deputies of the respective departments of these timber firms indicated that poor forecasting, lack of resources; lower morale, operating difficulty and time consuming process were the limitations that sometimes influence their budget preparation. Interestingly, 56 (63.6%) of the respondents indicated that difficulty to define objectives was one of the challenges that sometimes face timber firms in Kumasi while 32 (36.4%) of them sees it as never a challenge at all to them. From the results, it could be said that timber firms sometimes face some challenges during their budget preparation.

The poor forecasting as seen in this study may come about as result of uncertainty of certain conditions that affect the production, distribution and marketing of the products. These conditions may be inflation, shortage of raw materials and other economic situations that cropped up during the period of budget execution. This finding of the study is congruent with the assertion of Horngreen et al. (2000) who asserted that because of future uncertainties assumed conditions may not necessitate the revision of budgeted targets. Lack of resources and lower morale are always linked to production in organisations because due to economic theory of scarcity in relation to demand and satisfaction, there is always gaps left in achieving fully what organisations intend to achieve.

It was realised that challenges of budgeting is not only limited to its preparation but also its implementation. The study therefore examined challenges that are associated with budget implementation among timber firms in Kumasi. Further data were elicited from the respondents concerning the challenges of budget implementation among timber firms in Kumasi. Majority (more than 50%) of the respondents see month-to-month monitoring and operational difficulty as the challenges that often confront timber firms during the implementation of their budgets. They added that inability to adopt to suit a changing need, lowering morale and delays are also some of the challenges
that often confront timber firms during the implementation of their budget. The findings are in line with the comments of Chenhall (2003) who reiterated that the perceived environmental uncertainty has a much stronger impact on the implementation of the corporate budgeting system.

The third challenge of using budgeting system in an organisation as found in this study is related to human factors that affect budgeting decisions. Most of the heads and deputies of departments said that personal interest and negative work attitudes are the human factors that affect their budget decisions. The findings are in line with the assertion of Peirce (2004) who indicated that in order to avoid the human factor problems identified above which affect budget decisions, good attitudes which are the key to successful budgeting need to be developed among employees, where management explain to its staff that budgets are the most effective way of corporate planning and control.

5.1 SUMMARY

Budgeting and budgeting control measures are an integral part of any organisation including timber firms. It serves as a basis of planning, controlling cost of operations and evaluating performance of workers of the organisation. For a budget to be an effective one, sound organisational structure, research and analysis as well as management acceptance should be considered. Budgeting thus, serves as a blueprint for any organisation to follow in an up-coming period usually for one year period at most.

Despite the laudable benefits of budgeting, its preparation, implementation and execution need to be controlled and monitored to avoid deviations from the plan and serve as a basis for revising the budget put in place. Challenge of preparation implementation and human factors that tend to affect budgeting need to be given serious thought. In the preparation of the budgets, management should give serious thought to the external environment, emerging technologies, organisational structure and size as well as culture of the organisation and the setting where the timber firms operate.

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