

The Management based on Standards and Expense Budgets

M. N. Spînu

Marian - Nicu Spînu

Faculty of Economics

"Aurel Vlaicu" University of Arad, Romania

Abstract

The creation and the proper functioning of the organizations efficient structures depend on the knowledge one has of the normal consumptions and expenses in expense centers and compartments of structures. The comparison between the actual performances and the stipulations facilitates the appraisal and control of the accuracy of the costs employed on the principle of reverse connection. Consequently, the organization's managers can intervene in due time to eliminate the factors and causes that disturb the proper functioning of the economical and financial mechanisms.

Keywords: the system of managerial methods, cost standards and expense budgets, deviations from the stipulations, the management by objectives and the management by exceptions, the audit and the management control.

Introduction

The prerogatives of management can only be exercised by taking into account a group of managerial strategies and tactics which are defined in connection with a fundamental criterion. Thus, if the criterion consists of the company's objectives, we talk about "management by objectives"; if the criterion consists of the deviations between the actual performances and the purposes of the organization, we talk about "management by exceptions"; if the criterion consists of

the products manufactured, we talk about “management by product”; if the criterion is the cost, the management is “by costs and budgets”; in the case of large actions like the redesign of the firm or the adoption of Communicational and Informational Technologies, we talk about “management by project”, etc.

In fact, it can be stated that no pure managerial method can be used. It is a system of managerial methods adjusted to the organization and functioning of each business which appears to be more adequate.

Views on management based on standards and expense budgets

In the case of companies, the strategies and tactics adopted must take into account the organization’s objectives. In conformity with the requirements of the management by objectives, each stipulated objective must be associated with the person responsible and also with the authority of carrying the objective through. The efficiency of the triangle authority – responsibility – competence represents the condition for the company’s management to come closer to the purposes and performance of the entity along the perpetual route actions – information – decisions. Detailing the objectives at the level of jobs requires the establishment of the instructions to be followed in order to fulfill them. Moreover, the management by objectives involves the application of the standard costs method for the calculation of final products costs. This method makes it possible to timely determine the abnormal consumptions and expenses (the credit of the expense accounts comprises the direct expenses standards and the regulations for the indirect expenses, while in the debit the actual expenses are collected, expenses which, when they are incurred, are compared with the ones stipulated by standards and regulations).

As it is assumed in the management by objectives, cost standards are socially necessary levels of the consumptions and production expenses in normal conditions of technology and firm assets usage. Their usage in the informational and decisional processes provides managers with a powerful toll of cost control through the establishment of certain rules and corpora of rules that are to be reached in the internal processes of the organization. The standards are established at the level of the three great categories of production costs, namely the costs of raw material, labor costs, and general costs of production and administration.

The standards represent sizes and values established scientifically through modern methods of watching, recording and analyzing both the past events and the estimated elements that are planned for the period when they are going to be used. The standards reflect the expenses that are socially necessary for the unfolding of a particular process or phenomenon. At the same time, the management control requires the comparison between the standards and the actual results. This comparison is also needed in the case of management by exceptions. The managerial function of control can only be properly accomplished by comparing the actual cost and the standard cost at the level of each operation or responsibility centre for a particular period of time. The difference between the standard cost and the actual cost is called a deviation or an exception.

There are other advantages also attributed to the method of standard costs, namely stock planning, the assignment and leveling of manufacturing resources, the assessment of performance based on the system of responsibility management, the improvement of the stimulation systems, etc. The method presents a few disadvantages as well, namely the arbitrary interpretation of variations and the initiation of some less relevant intervention processes, directing the staff towards the reduction of variations instead of directing them towards the increase of the actions' efficiency, inefficient operational processes.

The management by exception is dependent on the knowledge of the deviations between objectives and actual performances. Consequently, each manager, according to his/her level, is assigned a sector in which it his/her responsibility to take decisions in order to correct the errors of functioning that might occur in that particular compartment. In the case of smaller deviations, the self-adjustment of the company's components' manifestation is the responsibility of the operative management, while the greater errors are the responsibility of the strategic and tactic management. This managerial method implies the existence of a rational informational system capable of providing "the exceptional situations", the determining factors and causes, and the necessary remedies.

According to the pre-established standards, in the case of management accounting three types of deviations are calculated: those of the direct costs of raw material, those of the direct costs of labor, and those of general expenses.

The total deviation of the cost of raw material consists of the difference between the actual cost of raw material and the standard cost of raw material. When the actual cost is bigger than the standard cost, the deviation is unfavorable. This deviation may be divided into two components: the deviation of the price of the raw material and the deviation of the quantity of the raw material, as both elements are taken into account in the calculation of the cost. The schematic representation of this deviation may be observed below:

The total deviation of the cost of labor is represented by the difference between the actual cost of direct labor generated and the standard cost of labor for the good units produced (the good units are represented by the difference between the total number of units produced and total or recoverable rejects).

The total deviation of the production general expenses is represented by the actual general expenses and the standard ones which are distributed to production by using standard lists. This deviation is divided into two parts: the controllable deviation of expenses and volume deviation of expenses.

The deviation of the quantity of raw material can be caused by various factors, namely by the inadequate quality control, by the inferior quality of raw material, by the violation of the consumption rate, by high specific consumptions, by a low quotient of material use, etc.

The deviations of basic salary may be caused by a larger increase in the remuneration than it was estimated, by the use of workers with a different qualification than the one required by the job, by the payment of bonuses, over-time and shifts, etc.

The deviation of the labor force's productivity is usually associated with the use of inferior raw material, with the use of new employees, with inappropriate working conditions, with the use of workers with a different qualification than the one required by the job, with the labor force's fluctuation, the significant weight of the medical leaves, etc.

The controllable deviation of the production general expenses may be caused by the overuse of the labor force in the functional and administrative structure, changes in overtime, unexpected price and tariff changes, increases in the unproductive expenses, etc.

The deviations of price are influenced by certain factors that affect the purchase price, namely the size of the purchased batches, the delivery method used, the discount system provided by the purveyor,

the quality of the purchased material, the dates of delivery, the taxation level, etc. If there are no changes in the market's functioning, it means that the unfavorable price deviation is the result of the managers' failure to find convenient purveyance sources. The management tends to control the quantitative variations more than the price variations.

The deviations' establishment contributes to the identification of the efficient and inefficient areas of activity, but the essence of an efficient control does not rest in simply identifying the deviations' size, but in determining the causes of this deviation and in establishing the proper corrective measures. The deviations' study facilitates the identification of the causes that lead to these deviations, the placing of responsibility in each centre, and the adoption of certain corrective or stimulating methods depending on whether the deviations were favorable or unfavorable.

The use of standards and the analysis of deviations become essential tools of management control. Of course, there are both advantages and disadvantages in using these means. Among the advantages we can note the following:

- the use of standards facilitates the implementation of the management by exception;
- standard costs facilitate the planning of treasury flows and of stocks;
- if practical standards are used, they promote efficiency and economy. Consequently, the employees become aware of such variables as time and cost. Moreover, standards represent a good system of providing financial stimulants;
- standard costs are more appropriate in the case of companies organized on responsibility centers (another management control tool).

There are some disadvantages connected with using standards as well:

- difficulties in establishing which deviations are noteworthy;
- if the entire management is centered around the deviations that surpass a certain level, then other useful information like the organization's analytical tendencies might be overlooked in the decisional process;

- on the one hand, if the managers' remuneration is dependent on the system of standards, some of them might hide, diminish, or even fail to report the unfavorable exceptions. On the other hand, the managers interested in the criteria of efficiency and economy, might take proper decisions in what the business is concerned, but might not benefit from positive results;
- with the implementation of standards and of the management by exception comes a transformation in the attributions of the supervisors often fail to visualize the entire process. Last but not least, standards, by establishing responsibilities, trigger a critical attitude towards the employees.

Regardless of these disadvantages, it may be concluded that the use of standard costs and the analysis of deviations given by the managerial accounting constitute strong points in exercising management control in a company.

The company's system of budgets represents the basic component in the proper exercise of the managerial functions of anticipation and control.

The budget, as a tool of the economical and financial activities' management, has the following functions:

- the function of anticipation, which is based on the fact that the budget represents the financial estimation of the levels of resources, of funds, and of expenses for all the economical and social activities that take place in a company;
- the function of control, which is exercised when expenses are incurred or conducted, when revenues as results of own activity are obtained, and when necessary funds are raised;
- the function of securing the financial equilibrium: the budget is used to conduct the balanced ratios between expenses and revenues.

The audit and the budgetary control, which consist of continuously comparing the results with the budgetary estimations, are performed with the help of the budgets. The purposes of the audit and the budgetary control are the following:

- to identify the factors and the causes of the budgetary deviations;
- to inform the managers and the administrators from different hierarchical levels;
- to create and carry out certain corrective actions;
- to judge the activity of various employees responsible for budgets.

In a company, the management monitors the activity by using a general budget which includes the operational budgets and the financial budgets. The operational budgets presuppose the estimation of the different types of resources, while the financial budgets offer the estimation of the company's financial resources, including the budget of the treasury activity, the estimated results account, and the estimated accounting balance sheet.

In the operational budgets of the companies with a production activity the following types of budgets are taken into account: sale budget, production costs budget, purchasing budget, human resources budget, General and Administrative budget, capital expenditures budget.

For many companies, the budget's main factor is the volume of sales and this constitutes the starting point for the budgetary process. The sales budget is a detailed plan, expressed in both physical and monetary quantities, which identifies the estimated sales of a product or a service for a future period (usually for a year).

The distribution activity budget is derived from the sales budget and it presents in detail all the expenses connected with the sales function of the company for a future period of time (usually for a year). The production costs budget is a detailed plan which presents the quantities and costs of each product and service that is to be manufactured or offered in order to satisfy the budgetary stipulations regarding sales and inventory needs.

The purchasing budget is a detailed plan that identifies the number and schedule of raw material and other types of materials that are to be purchased in order to satisfy the needs of the production process. The human resources budget identifies both the labor force needs for a future period of time and the salary expenses connected with the needs.

The indirect costs budget presents the production costs that need to be conducted in order to carry out the stipulations connected with the

production process for a future period of time. Such expenses as the raw material costs and labor force costs are not taken into consideration.

The General and Administrative budget offers a detailed plan of the working expenses necessary for the carrying out of the company's general activity in the future. Such expenses as those connected with the production and merchandising functions are not taken into account.

The capital expenditures budget presents in detail the sums and schedule of the capital expenditures estimated for the future. The information connected with capital investments influences the budget of the treasury activities and the balance of the fixed assets accounts from the estimated accounting balance sheet.

The budget of the treasury activities represents a projection of the revenues and payments of cash resources for the future and has two main purposes: it provides the final balance of the cash resources which is necessary in order to draw up the estimated accounting balance sheet, and it shows when gluts of money or gaps of cash resources are recorded. The estimated results account follows the accounting principles and it regroups the expenses and the revenues according to their nature, thus influencing the estimated accounting result. The estimated accounting balance sheet includes the results of all the other documents presented. A synthesis of the budgetary system can be read below:

In the companies' overall competitive environment, the budgetary system has an extremely important role as the economic efficiency of the organization's activity depends on it. The management cannot have a clear image of the company's financial evolution unless they have a perfectly coordinated budgetary system.

Fixed budgets have certain limits when it comes to comparing results because the volume of activities might vary. Consequently, flexible budgets have been introduced. They allow the company's current activities to be monitored. A flexible budget, as opposed to a fixed budget, presents the budgeted cost levels for the current activity's level. The flexible budgets offer the possibility of estimating the costs for a larger number of relevant levels of activity. These estimations are presented as scenarios of evolution. The budgets' drawing up and control are a clear necessity, regardless of the size of the company as its efficiency and proper functioning are dependent on them. In other words, the budgets are the management's most important tools with which they can measure the firm's performances.

The budgetary control is conducted monthly and it answers two objectives:

- it identifies the favorable or unfavorable deviations from the budgetary stipulations by performing the budgets' execution control; in this case the management control deals with past events;
- it readjusts the budgetary estimations and it imposes corrective measures; in this case the management control deals with future events.

Conclusion

The standard costs' system is a result of the attempts to establish a standard of value in relation to whom each performance might be measured. The cost control is carried out at the same time with the deviations' establishing and this helps the manager take efficient and rapid decisions.

The mission of the budgetary control is to identify and to explain the deviations from the budgets' stipulations. The analysis of the deviations is complemented by a combination between the firm's management – an example is represented by the management by exceptions (the control of the deviations that surpass a certain level is one of the attributions of the manager) – and management by responsibility – in this case some employees must take full responsibility for certain deviations from the budgets.

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