ACTIVITY BASED BUDGETING

Meaning:
The term activity based budgeting (ABB) is defined as the process of planning and controlling the expected activities of the organization to derive a cost-effective budget that meets forecast workload and agreed strategic goals. The Activity based budgeting is a quantitative expression of the expected activities of the firm, reflecting managements forecast of workload and financial and non-financial requirements to meet agreed strategic goals and planned changes to improve performance.

Key Elements:
Following are the three key elements in activity based budgeting:

1] Type of work/activity to be performed,
2] Quantity of work/activity to be performed,
3] Cost of work/activity to be performed.

Activity based budgeting mainly focuses on the activities or business processes. Resources required are determined on the expected activities and workload. The objective is to bring in efficiency into the system. So, in the process of budget preparation, many key questions, such as following need to be addressed and properly answered:

- Is the activity necessary?
- Is it possible to club a few activities to bring in efficiency?
- Does the activity in question add value to the customer or increase profit to the firm?
- How much resources are to be allocated?
- Is this the best way of performing the activity?

Steps in Activity Based Budgeting:
Following are the essential steps involved in the activity based budgeting process:

1] Formulating strategies for the organization consistent with the needs of the customer.
2] Developing plans to translate strategies into activities.
3] Identifying the activity levels for each activity.
4] Forecasting workload for carrying out the activities.
5] Estimating resources in time, cost and quality for each activity level, thus formulating budget frequently for each activity.
6] Ranking the budget requests.
7] Finalizing the budget by approving the budget requests in the order of ranking.

Activities may be evaluated by classifying them as ‘current level’ and ‘i level’ resource utilization. Budget requests may be ranked by looking at the value (benefit) to the customer and cost to the firm for various levels of activity.

**Advantages of Activity Based Budgeting:**

1] ABB helps formulate strategies to sustain competitive advantage.
2] When ABB is followed control on activities is facilitated. Ineffective or non-value creating activities can be cut down through analysis.
3] It helps to improve the performance of the firm due to linked strategies.

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