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Use of Budgets in Organisational Performance Evaluation

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ABSTRACT
Performance evaluation is a management tool for internal control and is pivotal to an organization. Performance evaluations of the organization in terms of financial and non-financial assets are crucial in allocation of resources and achieving cost efficiency. This study focused on use of budgets for performance evaluation in organization by specifically examining the influence of planning on performance evaluation. It is a library type of research. Information used were obtained from textbooks, journal articles, seminar papers and conference papers which was achieved through the review of related literature. Based on outcomes of the review of extant studies, it is revealed that budget planning is a critical factors that could enhance performance. It therefore recommended that there should be proper budget planning based on the goals with full management participation taking cognizance of the entire units in terms of cost, profit and investment issues for the purpose of performance evaluation.

KEYWORDS: *Budgets, Planning, Performance Evaluation*

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I. INTRODUCTION

In today's corporate business world, managers of units, subsidiaries and sections are evaluated from time to time in order to assess their level of performance in the organization. Performance evaluation is a management internal use and is pivotal to an organization. Egbunike and Unamma (2017) noted that performance evaluation is a tool for appraising how well an organization has performed. According to Ogiedu, Eragbhe and Ibadin (2009), performance evaluation is a key component of corporate firms and managerial control system in any organization. These include gathering, summarizing, and analyzing information to determine whether goals are being achieved, and to prescribe the actions required to further those goals. Juraj and Nataliia (2017) noted that in performance evaluation, inputs which are resources used to produce an output like salaries, labour hours, material costs, depreciation, etc), outputs and outcomes are essential issues to be considered. A firm's performance evaluation system is considered as an important part of its financial control system of the organization internal operation.

Budgeting, which is a tool of planning and control is indispensable for performance evaluation. Egbunike (2014) believed that budget is a comprehensive and coordinated plan expressed in financial terms for the operations of an enterprise for some specific period in the future. Budgets have taken on different roles, becoming tools for bargaining and allocating power, for planning and controlling, for providing impulses to the economic and social environment, and for ensuring transparency and stakeholder involvement (Sicilia and Steccolini 2017; Saliterer et al. 2018). Kapler (2007) noted that the use of budgets for performance evaluation measure purposes, firms' managers assess cost implications and describe the efficiency of various activities. With the use of budget in performance evaluation, managers need not only data on output, they also need reliable cost data. And these cost measures have to capture not only the obvious, direct costs of the units, sections and subsidiaries, but also the hidden, indirect costs. Budgets require management to specify expected sales in the case of a market organization, cash inflows and outflows, and costs (Horngren, 2006). Also, managers of firms allocate people to the activities with the highest productivity per person.

Budgets and evaluation as a way of assessing an organization or programme is to evaluate its internal operations and to conduct such a best-practice, which requires some process measures—appropriate descriptions of the organization's key internal operations that can be compared with some operational standards. Budget is a statically financial plan or blueprint, while the term "budgeting" refers to the act of preparing a budget or the activities of predicting and qualifying future requirements for finance (Garrison, Noreen, & Seal, 2003). Successful budgets require managers' participation, proper planning, controlling and goal clarity in order to ensure effective and efficient performance evaluation.Joshi (2003) believes that through budgeting in the process of financial decision-making and internal operation of organization, multiple functions regarding budgeting behavior can be achieved. These functions are planning, coordinating, communicating, control, and evaluating. With performance evaluation managers could know if operations meet with the objectives of the

enterprise. Hence this study conceptually reviews the use of budgets in performance evaluation in corporate organizations.

The use of budgets in performance evaluation has been a major concern of management of organizations. The proper measurement of the performance of an individual, a division, a subsidiary, or even a company as a whole is not simple. The main reason for this is that different bases of evaluation result in different measures of performance; that is how you choose to keep score affects the final score. There are many events affecting performance that are not controllable by the section, unit or subsidiary. Also, a major issue is that planning have not been given adequate attention in the budget for the purpose of performance evaluation and such could have negative implications on the outcome. Several studies in the use of budgets in performance evaluation in private organizations were carried out in developed countries like USA, Britain, France, China (Kapler, 2007; Drury, 2000;O'Connor, Chow & Wu, 2004), while few of the studies were from developing countries like Nigeria (Ogiedu et.al, 2009; Kazeem & Darrell, 2012;Abdullahi & Unegbu, 2012). This study introduced planning which to the best of our knowledge have not been given attention by extant studies from Nigeria.

The broad objective of this study is to investigate the use of budgets in performance evaluation in corporate organizations, while, the specific objective is to:

Determine the effect of budget planning in performance evaluation in firms.

II. LITERATURE REVIEW

Conceptual Review

Performance Evaluation

Performance evaluation arises as a result of functioning of different components in the organization. It is imperative that the different components that make up the organization are functioning properly (Ogiedu et.al. 2009). Performance Evaluation is a key mechanism for improving firm's management. According to Kalali (2011), performance can be evaluated or measured in both financial and non-financial. Financial performance is generally defined as the use of outcome-based financial indicators that are assumed to reflect the fulfillment of the economic goals of the firm (Murphy, Trailer & Hill, 1996). Financial performance refers to the degree to which financial objectives are being or has been accomplished. It has been widely used to measure business performance in small and large firms. A great deal of accounting literature (Lau & Sholihin, 2005) recognizes the inherent advantages of financial measures. They argue that financial measures might be beneficial because they are objective and certain to provide a summary view of the success of the organization's performance and operating tactics.

Kaplan and Atkinson (1998) consider financial measures as the traditional, most widely practiced, and popular management accounting tool because they focus on "what matters most in most organizations—profitability". Financial measures consist of a wide range of dimensions, but efficiency (such as return on investment, return on asset etc.), profitability (sub-dimensions include return on sales, net profit margin, gross profit margin etc.), and growth (such as sales growth, market share growth, change in net income etc.), are the commonly chosen output measures. Sales revenue and return on investment are the most frequently used financial ratios.

Besides financial measures, non-financial measures (also called operational performance measures), such as employee's job satisfaction and managerial performance etc., are defined as a broader conceptualization of organizational performance (Hofer & Sandberg, 1987). Otley (2003) suggests that, when monitoring firm performance, managers tend to place relatively less emphasis on traditional financial measures of performance such as return on investment or net profit. This is usually explained in terms of traditional performance measures (the accounting-based measures or financial measures) which is unable to satisfactorily reflect firm performance affected by today's changing business environments (Hoque, 2004).

McKiernan & Morris (1994) criticize the fact that the measures of financial performance cannot accurately measure organizational effectiveness or total performance. largely supports claims that since non-financial performance measures focus on a firm's long-term success factors such as customer satisfaction, internal business process efficiency, and innovation, they can best capture the overall performance of organization. Therefore, a multi-dimension system of performance measures combining financial performance, non-financial performance, and managerial performance is used to reflect the overall performance of firms.

Budget

Budget is concerned with direction of things. Libby and Lindsay (2003) noted that budget is a detailed and quantitative plan. It shows the information about the acquisition and use of financial and other resources over a specific time period, either a long-range period (two- to ten-year) or a short-term period (one- to two-year, or monthly, or daily-based). Budgets require management to specify expected sales in the case of a market organization, cash inflows and outflows, and costs (Horngren, 2006). Lucey (2003) defined a budget as a

quantitative expression of a plan of action prepared for an organization as a whole in order for them to carry out certain functions such as sales and production or for financial resources items such as cash, capital expenditure, man-power purchase and others.

Budgets provide rational and tangible data facilitating and enabling decision-making of organizations. Instead of expressing a budget as a statically financial plan or blueprint, the term "budgeting" refers to the act of preparing a budget or the activities of predicting and qualifying future requirements for finance (Garisson, et al., 2003). According to Lambe, Lawal and Okoli (2015), budgeting is a key policy instrument for management and management of firm; it is a familiar activity to many as it is practiced in our private lives as well as in businesses, government and voluntary groups. Some management accounting theorists (like Drury, 2000; Joshi, 2003;) believe that through budgeting in the process of financial decision-making and internal operation of organization, multiple functions regarding budgeting behavior can be achieved. These functions are planning, coordinating, communicating, control, and evaluating. If administered wisely, budgeting (a) compels management planning, (b) provides definite expectations that are the best framework for judging subsequent performance, and (c) promotes effective communication and coordination among various segments of the organization (Horngren, 2006). . Kpedor, (2012) stated that budget as a profit planning device sets standard of performance of managers, while budgetary control is a tool implored by management to keep track of actual performance to ensure budgeted standards are met.

Budget Planning and performance evaluation

(Douglas, 1994) budgeting planning (budget-setting or budget preparation) refers to developing quantitative goals of the organization and preparing various budget. Business organizations use long-term budgets to lay out the planned financial goals and actions over periods ranging from two to ten years. Long-term budgets are part of an integrated business strategy that along with production and marketing plans, guides the firm toward strategic goals (Gitman, 2006). So in this regard, long-term budgets are closely related to strategic plans. Capital budgets, as one example of long-term budgets, are emphasized in financial accounting and budgeting literature. Capital budgeting is defined by Garisson et al. in 2003 as a type of investment decision-making used to describe how managers plan significant outlays on some accounting literature (McLaney & Atrill, 2002; Garrison, 2003) group the strategic plan directly into one of long-term budgets in business organizations.

It details the planned expenditure for facilities, equipment, new products, and other long-term investments. The complete capital budgeting process involves a series of actions, including generating investment project proposals consistent with the firm's strategic objectives, estimating after-tax incremental operating cash flows for the investment projects, evaluating project incremental cash flows, selecting projects based on a value-maximizing acceptance criterion, reevaluating implemented investment projects continually, and performing post audits for completed projects15. Apart from long-term budgets, short-term budget are used to guide day-to-day operations. Short-term (operating) budgeting specifies the acquisition and use of financial and other resources over a short-term period, which most often covers a 1- to 2-year (Garrison et al., 2003). It is expected that with proper budget planning taking cognizance of the entire units in the organisation, performance evaluation can be achieved.

Theoretical Framework

This study is fastened on theory of the firm initiated by Coase 1937. In his article, Coase (1937) attempts to explain the functions of the firm and to explore what make the firm a better means of managing production than the market and concluded that economic efficiency or cost reduction is essentially the reason behind the firm's existence. This research pays special attention to use of budget and performance evaluation in explaining what situations firms reduce production costs and why transaction costs are lower in some firms than in others. Kapler (2007) gives a wide survey of all potential factors influencing the transaction costs of a firm and concluded that more costs are incurred in some firms than in others, the previous research (Foss, 2000; Stoelhorst & Van Raaij, 2002; Choo & Bontis, 2002) emphasized the theory of performance differences between firms. Foss (2000) suggests a more direct relationship to the performance difference between firms, when different costs of firms are observed.

This theory was adopted for this study because relates it relates to cost reduction

Empirical Review

Wijewardena and De Zoysa (2001) perceive that the impact of budget planning and budgetary control on performance in SMEs in Australia. Data was collected from two thousand manufacturing SMEs in Australia. The results show a positive and significant relationship between budgeting planning and sales growth, and between budgetary control and sales growth. However, no significant difference was found between budget planning and return on investment (ROI), nor between budgetary control and return on investment.

Sugioko (2010) carried out a study on “the impact of budget participation on job performance of University Executives: a study of APTIK- member Universities in Indonesia”. This research aimed to test empirical evidence regarding the role of mediating on the impact of budget participation on job performance. The study concluded that budget participation has a positive and significant impact on job performance.

Kpedor, (2012) examined budgeting, budgetary control and performance evaluation system of Allterrain Services Group in Ghana. The main instrument was administration of the questionnaires. The analysis of the findings indicated that most of the key actors do not work with the budget due to lack of proper induction and proper role profile of the office they occupied.

Mohammed and Ali (2013) in a study “the relationship between budgeting and performance of Remittance companies in Somalia” concluded that the correlation between budgeting and firm performance is 0.514, which means that one level increase of budgeting effectiveness will lead to 0.514 higher firm performance. The probability of this correlation coefficient occurring by chance is 0.00. This coefficient shows that a statistically significant moderate positive relationship between budgeting and firm performance.

Egbunike and Unamma (2017) examined budgets , budgetary control and performance evaluation of hospitality firms in Nigeria. The study employed descriptive design and primary data (questionnaire) was the major source of data collection. The data obtained were analyzed using both descriptive and inferential statistics. Findings indicated that budget and budgetary control could serve as an avenue through which hospitality firms in Nigeria can be evaluated. In addition, it was revealed that there is a significant variation in the budget, budgetary control and performance evaluation of hospitality firms in Nigeria.

III. METHODOLOGY

It is a conceptual study by making use of library type of research. Secondary source of information are employed. The information for the conceptual study were obtained from textbooks, seminar papers, journal articles and conference papers. This was done by searching related literature and proper critic of the issues especially in connection with the specific objectives. All information from various related studies formed basis for findings, conclusion and recommendations.

IV. CONCLUSION AND RECOMMENDATIONS

Budget is critical issue in any organizational settings. Budget is designed to address boiling or burning issues which are expected and suitable for performance evaluation. Whenever budgets are carried out there are tendencies that issues in the organization needed to be given attention. Budget needs adequate planning, control and goal setting in order to achieve the stated objectives.

For organization to carry out focused budget capable for performance evaluation which can be in both financial and non financial measurement, information sharing between subordinate and superior is necessary during budget discussions. Therefore, use of budget in performance evaluation can facilitate the achievement of the internal organization stated goals and objectives within the time period.

Having examined the entire work, the following recommendations are put forward.

(1) There should be proper budget planning taking cognizance of the entire units in terms of cost, profit, investment and issues in relation to employees for the purpose of performance evaluation.

(2) There should proper control of the planned budget such that it can be suitable for performance evaluation.

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