

ICFE Test of Reading - Sample Part 6 Task

Questions 49 – 54

Read the following extract from a text about budgeting and the questions on the opposite page. For each question 49 – 54, mark one letter (A, B, C or D) on your answer sheet.

COMPANY BUDGETS

Most senior executives know that the competitive battles ahead will involve not only ensuring that their company gets better at what it does, but is also different from others. To achieve this they need talented managers who can produce more imaginative strategies for growth and improvement, make faster decisions, be more flexible, be better prepared to anticipate threats and opportunities, and who can consistently improve quality and customer satisfaction. To this list you can add any number of other key competitive issues that are becoming more important as the service economy gathers speed.

But executives also know that none of these aspirations are attainable without changing the way the business is run. While most companies have tried to address these issues by reducing management layers and focusing on the customer, few have been successful. One of the reasons is the inability to shift the management philosophy from one of top-down control to bottom-up empowerment. It is because budgets are most commonly used by organisations to exercise control that they are at the centre of this thorny issue.

Budgets are, in effect, barriers to change and fail to do well what most managers think they do well – that is, provide order and control. They are barriers for many reasons. Firstly, they reinforce the command-and-control management model and thus undermine attempts at organisational change, such as delegation and empowerment. In addition, they tend to set a ceiling on growth potential and a floor for cost reductions, thus stifling real improvement breakthroughs. Strong brands, skilled people, excellent management processes, strong leadership, and loyal customers are assets that are outside the measurement orbit of the accounting system. Budgets are typically extrapolations of existing trends, with little attention being paid to anticipatory models. What is more, they act as barriers to exploiting co-operation across the business units.

If asked why we use budgets, most managers would probably answer, 'to set targets and control business operations'. But budgets evolved in the 1920s to help growing businesses manage their capital resources and plan their cash requirements. It was not until the 1960s that budgets were used to set targets, control operations and evaluate managerial performance. While planning remains an important part of the management process, it is widely believed that setting targets and controlling and evaluating performance using budgets is fundamentally flawed because it directs managerial behaviour towards achieving predetermined financial targets rather than harnessing the energy of people at all levels towards continuously improving competitive strategies and customer-oriented processes.

So, if existing budgeting systems have such crucial weaknesses, why do we still rely on them? In fact, accountants have tried to improve them. Zero-based budgeting and activity-based budgeting represent valiant efforts to update the process, but they tend to be complex project-driven approaches that fail to evolve into standard management practices. Basically, though, budgeting has not changed because it is a part of unchallenged tradition. Some companies are re-engineering their budgeting processes to make them faster and cheaper, but such an approach fails the test, as it leaves the behavioural weaknesses in place.

What does all this mean for the role of management accountants? Many accountants now accept that setting fixed financial targets and measuring performance against them makes little sense when the competitive environment is subject to continuous change. Plans and strategies need to unfold continuously as new knowledge emerges. Above all, management accountancy should be concerned with the future and ensuring that the right questions are asked and the right decisions are taken that add maximum long-term value. It is hard, though, to see how these changes can be managed successfully while leaving the current budgeting system in place.

- 49** To deal with the competition they are likely to meet in the future, companies should look for managers who will
- A** recognise and reward talented people.
 - B** bring considerable experience to the job.
 - C** respond immediately to financial difficulties.
 - D** take a creative approach to developing the business.
- 50** According to the second paragraph, why have companies failed in their response to key competitive issues?
- A** Authority for decision-making is too restricted.
 - B** Customer needs are not given sufficient priority.
 - C** There are too many layers of management.
 - D** Budgets are not adequately monitored.
- 51** One problem resulting from the way budgets are usually set is that
- A** they give too optimistic a view of a company's growth potential.
 - B** they allow staff to avoid taking responsibility for their decisions.
 - C** they tend to produce too many targets for the workforce to meet.
 - D** they limit innovative behaviour because they focus on past experience.
- 52** According to the writer, changes in the use of budgets since the 1960s have prevented managers from
- A** giving enough time to planning.
 - B** concentrating on motivating the workforce.
 - C** working out realistic targets.
 - D** assessing the competence of their employees.
- 53** According to the writer, why have new budgeting systems not been widely adopted?
- A** Traditional systems are relatively easy to operate.
 - B** New systems have proved slow and expensive.
 - C** Traditional systems are part of accepted practice.
 - D** New systems have proved unpopular with managers.
- 54** According to the final paragraph, many management accountants now believe that
- A** companies should be prepared to modify their strategies.
 - B** budgeting should not influence management decisions.
 - C** too many company decisions are taken with a short-term view.
 - D** targets should reflect recent trends in an industry sector.