Zero-base budgeting—an attempt to reevaluate all programs, activities, and expenditures in terms of cost-benefit.

ZBB FITS DP TO A TEE

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ZBB does not supplant the corporate budget. It is not suited to all organizations nor all activities of an organization.

In preparing decision packages, a unit manager begins with the specification of the unit's objective and purpose. After a description of how the unit currently operates and the resources utilized, the manager then develops workload and performance measurement techniques, considers alternative methods of operating, and performs incremental analyses. The final decision package will be placed in one of the following three support level categories: (1) different methods of reduced levels of effort to do each activity, (2) "business as usual" levels of effort, where there are no other alternatives; (3) new activities and programs.

Once the manager has defined all the obligatory and discretionary activities into packages, a ranking process occurs. Usually the manager ranks all packages in order of decreasing benefit to the company on a cost-benefit basis. This ranking activity begins at the cost center level. A committee is formed by all managers in the cost center. The committee reviews all the packages presented to it and ranks them in importance by means of a voting mechanism. The packages considered most beneficial to the company as a whole receive the highest rankings, while the least important receive the lowest. A cut-off point is now established. Given the general level of funds available in the coming fiscal year, all packages above a given ranking are accepted by the group and all those below a certain point are rejected.

These decisions are then passed up to the next higher management level. Here the manager reviews the rankings to determine if they fit into the organization's goals and to decide whether the rejected packages offer enough benefits to expand the level of funding. Upper managers briefly examine only a pre-established percentage of the packages to control volume. The process is repeated until all the accepted activities are filtered through to the top of the organization, where the budget for the entire organization is then created.

ZBB does not supplant the corporate budget. It is not suited to all organizations nor all activities of an organization. It has little use in budgeting for production costs such as direct labor, direct materials, and direct overhead, which are largely determined by production and sales volume. It is mostly applicable to the service and support area of an organization which has discretionary costs.

The purpose of this paper is to describe the application of ZBB to the corporate sector in Japan. It was modeled after the initial venture in Texas Instruments in 1971 which began in Texas Instruments' central laboratory and development efforts. Texas Instruments was so impressed with the results that they decided to spread the concept throughout the company and to describe a future relationship between the business and corporate management departments.
The request of additional reductions of manpower was greatly facilitated by the use of ZBB. The user departments, typically the loneliest complainers of poor service and high costs, accepted further reductions in service levels because they participated in the prioritization of activities and benefited from lower charges. Management should, for the first time, properly evaluate the cost and necessity of any given activity. The activities with a ranking of 5 were eliminated mostly because of the desired reduction in positions but would probably be the last to be added should the need arise.

ZBB is typically used in the fall of each year in preparation for the annual budget. Because of the tremendous effort required in developing decision packages, it is recommended that after the initial analysis of activities is completed an annual update of the decision packages be made, thus eliminating much of the clerical effort. Each package should be ranked again according to the current priorities of the company.

The result of identifying and classifying all activities within systems and programs has been so helpful that it was decided to maintain those packages and prepare additional ones for newly identified activities. This process would supplement a project initiation request procedure that controls system change requests. Managers and staff are encouraged to add new activities to the system even though they might be blue-sky (in this industry, wild ideas tend to become reality within a short period of time).

The evidence of past applications of ZBB indicates substantial value in the concept of reevaluating budget programs and activities to determine relevant costs, benefits, and alternatives. ZBB has been successfully implemented in a growing number of service industries. Obviously, many of these companies feel that the benefits of ZBB outweigh the costs of increased time and effort. The benefits include the greater understanding of how funds are being used, increased participation of lower management in budgeting, and elimination of inefficient programs. However, because the budgeting tool involves the costs of increased time, paperwork, and effort, the implementation decision must be carefully considered.

ZBB is not, and should not be considered, a panacea for management’s budgeting problems. The technique should not be built up to promise more than it can realistically provide. In order to apply ZBB successfully, the following guidelines should be observed carefully:

1. Review the ZBB methodology and determine its appropriateness.
2. Analyze the need for your organization before implementing ZBB; that is, one should ask, “Is my organization ready for ZBB?”
3. Define resources required before implementation. This includes obtaining adequate staff for the budgeting department, setting up a top-management steering committee, and appointing local budget coordinators.
4. Sell high-level management on ZBB in advance of its implementation.
5. Long-range or strategic planning should always precede ZBB.
6. Develop a ZBB method, including: a review procedure, tailored to your organization’s environment.
7. Allow adequate time for training budget personnel and users.
8. Communicate to all levels of
EDP SPECIALISTS
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