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# The Study of Budget on the Basis of ABC and ABB Activities

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## Abstract

The cost system based on activities ABC is one of the important modern technologies and has a large share of theoretical studies and foreign and Iraqi applied research. Since this system exists, it is subject to many research and studies to derive from it new techniques and tools that would support the provision of appropriate information for management to be used in areas Many of them make decisions, measure and evaluate performance. The problem search continued economic units in the region of Kurdistan in the traditional follow methods in measuring the cost of their products which resulted in the emergence of many problems when determining the cost of products. The objective of the research is to clarify the general requirements and steps for applying modern methods ABB and ABC. Learn how to deal with indirect costs under the use of the cost system based on ABC activities. The importance of this research as sheds light on the importance of the system cost based on the activities of ABC are not limited to achieve the accurate measurement of the costs, or offer of detailed information, but extends it represents a sound basis for the management of activities and processes of economic unity through integration with some of the methods and administrative techniques Modern as TOM, ABB, JIT. The ABC system divides the economic units into sub-activities and analyzes them and knows how they consume costs and the extent of their contribution to the production process, which leads to a reduction in costs by knowing which activities add value or do not add value to production and dispense with activities that do not add value. The ABC system of cost-based activities assists management in making appropriate management decisions based on more realistic costs, which are useful in various fields such as those related to pricing.

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## Introduction

Cost systems have been subjected to many criticisms regarding the appropriateness of methods and procedures for measuring the cost currently used in light of the development of the modern industrial environment and the use of advanced technology in production, as traditional cost accounting procedures that measure the cost of products and prepare budgets for the company as a whole are unable to develop information more accurately Given that the bases for charging and allocating costs on products are not fair, especially with the significant increase in the proportion of indirect costs in the environment that adopts modern technology and thus not providing the appropriate information for management in order to skip Control, monitoring, monitoring and developing the work permanently. All this led to the interest of companies in many countries of the world such as the United States of America and some European countries and Japan to study and develop their administrative and accounting systems in order to control costs and increase efficiency and achieve profits, which led to the emergence of new systems and approaches to measure, plan and control costs in response to cost accountants. The need for more accurate and detailed information on the one hand and to address some of the problems experienced by traditional systems on the other hand. The cost system is based on ABC activities and the budget is based on ABB activities of these systems. The problem search continued economic units in the region of Kurdistan in the traditional follow methods in measuring the cost of their products which resulted in the emergence of many problems when determining the cost of products.

## Literature review:

The cost system based on activities ABC is one of the important modern technologies and has a large share of theoretical studies and foreign and Iraqi applied research. Since this system exists, it is subject to many research and studies to derive from it new techniques and tools that would support the provision of appropriate information for management to be used in areas Many of them make decisions, measure and evaluate performance. The study of Nassar et al. (2011)in his study focused on the application of the ABC system in the Jordanian (Phosphate Mines Joint Stock Company) company. The problem of the study was the lack of accurate allocation of costs and the extent of the impact of this on some of the company's decisions. This study proved that this system provides a positive contribution and has a great role in Many of the company's activities, including knowing the activities that contribute to the production process and knowing the activities that do not add value for the purpose of excluding them in the production process and thus this process contributes to reducing costs as well as reducing the time and effort required in carrying out the operations Productivity.

In a surprising study by Shaker Al-Sheikhly (2008) this study aimed to analyze the actual reality of caliphal accounting systems in the Iraqi industry environment for the General Establishment for Woolen Industries / Lab (July 30) to know how to control costs and the extent of their contribution to reducing costs by using modern methods of costs through removing activities that It does not add value to the factory, ABC system was applied to the factory, and costs were reduced by (13) million dinars compared to the traditional cost system. In the study of the other, Adams (2004), this study focused on the design of the ABC system and its application in the Iraqi Commercial Bank. The problem of the study is the absence of a caliph system, or the use of one of the traditional caliph systems, that may lead to distortions in the structure of the basic elements of the cost of the service provided by the bank is a sample of the study, which leads to weakening of control over costs and taking improper decisions, especially decisions based on verbal information in making them. This

study has proven that the ABC system can allocate a greater part of the costs to activities from the traditional Calvinist systems, as it reached The ratio of the assigned costs to the total cost under the ABC system in the Commercial Bank of Iraq / the main branch is 79.25%, while this ratio according to the traditional Caliphate systems reached 42.5%, an increase of 36.75%, and this increase came due to the allocation of direct costs only in light of the traditional costly systems, While a portion of the indirect costs was allocated to the activities benefiting from and causing them, as well as direct costs under the ABC system, through the use of cost directives.

**Objectives of the Study**

The research aims to achieve a number of goals, the most prominent of which are:

1. Clarify the general requirements and steps for applying modern methods ABB and ABC.
2. Learn how to deal with indirect costs under the use of the cost system based on ABC activities.
3. How to prepare a budget based on ABB activities.

The importance of this research as sheds light on the importance of the system cost based on the activities of ABC are not limited to achieve the accurate measurement of the costs, or offer of detailed information, but extends it represents a sound basis for the management of activities and processes of economic unity through integration with some of the methods and administrative techniques Modern as TOM, ABB and JIT.

**The concept of a cost system based on ABC activities**

The cost-based system has been developed to address problems arising from the application of traditional cost systems in economic units characterized by the extensive use of production technology. Many writers point out that the idea of a costing system based on activities is not a new idea. Many interested in accounting sciences have long since been aroused. For example, Drury notes that at the end of the first half of the last century, some writers touched in one way or another on the concepts of cost on the basis of Activities. The company General Electric may be the first company to have used a technology similar to the cost-based system of activities, as the company's controllers 'team (in an attempt to control the indirectly growing costs in the company) in 1963 proposed a new technology to calculate costs based on the activities being that It caused melasma (Al-Mikhlafi, 2002; Ahmed et al. 2019). Whatever the idea of a cost system based on activities is old or modern, the important thing is that its entry into force and use it in important administrative aspects such as profitability analysis, pricing and process development was not only in a series of articles was able to make cost ideas based on ABC activities are understandable and applicable. Cooper and Kaplan, (1988) The real challenge, Kaplan believes, is how to design internal accounting systems be able to support the strategy of economic unity in the light of the modern industrial environment and in the long term. Fakhz and Al-Dulaimi, (2002) from the previous definitions, we note that there are different opinions about the nature of ABC, some of whom considered it a system, and some of them considered it a method or method. The researcher believes that the ABC is an integrated system that possesses all the components of the system from Input inputs (represented in the ABC system on the financial data represented by cost calculations, and non-financial data represented by information related to cost guides) and Process operations (which includes sports treatment operations and are done in the activity centers to extract Unit Cost), Output (represented by distributing the costs of these activities to cost targets) and finally, Feed Back [which is the decisions that will be taken to correct deviations]. In addition, even if it does not rise to the level of being an integrated caliphate system, it can be called a sub-system for allocating indirect and direct costs that work under

the accepted cost systems, which are essentially part of the integrated accounting system for economic unity.

**The concept of cost system based on the activities of ABC, Horngren, et al., (2000)**

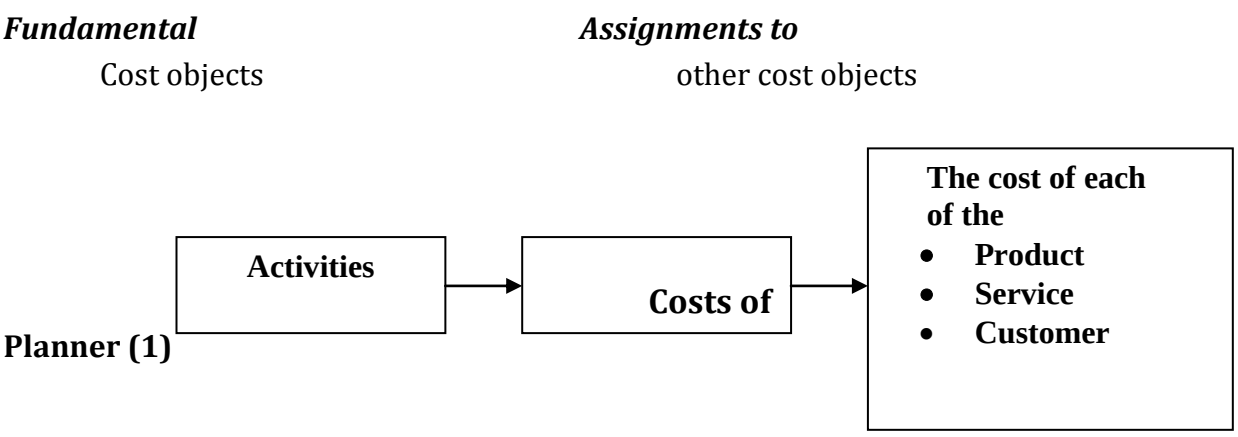


**Figure (1) Concept of the ABC System**

**The theoretical side of the budget on the basis of activities ABB**

The book defined budget on the basis of activities, each according to their scientific and intellectual direction, Cooper and Kaplan (1998) defined it as "a method whereby the resources needed to perform the activities in the facility are planned for a period of time so that they can rationalize the real spending according to what is estimated to perform these activities." Horngren et al. (2002) defined it as "a cost-focused approach to activities necessary to produce and sell products and services." Al-Marai, (2003) defined it as "a budget preparation method that uses the activity cost hierarchy to establish a budget for material inputs and costs as a function of planned activity". Mechanically, they are usually similar to the budgeted outputs/inputs method, where material inputs and costs are budgeted as a function of planned activity. Another defined it as "forecasting the total costs of products and services provided to consumers".

According to the foregoing, the researcher believes that the budget can be defined on the basis of activities as "a method by which the budget is prepared for each activity that adds value independently of the activities." Other necessary to produce and sell products and services. Once the economic unit implements the ABC system, it can use the ABC system information in the activity-based budgeting process. Where the goal of preparing the budget on the basis of activities is to authorize the processing of only those resources that are required to meet the production and volume of sales in the budget, while the cost system on the basis of activities assigns resource expenses to activities and then uses the activity cost guide to set the activity costs to cost goals (such as goods or services or customers), and so on The preparation of a budget on the basis of activities is the inverse of this process since the cost goals are the starting point because its outputs in the budget will determine the necessary activities that are used later to estimate the resources required for the budget period (Drury, 2006: Prabhu et al. 2019). The preparation of the budget on the basis of activities makes managers view fixed costs as a variable in the medium to long term, to use the term "committed cost" because managers have been committed to providing resources in advance and will not change their preparation in the short term due to fluctuations Short-

term demand, in other words, fixed costs are fixed due to management decisions and managers have the flexibility to redistribute those resources as conditions change. It should be noted here that indirect costs (including fixed costs) and indirect industrial costs are not presented as separate budget lines, they are not separable and should not be subject to customer purchase decisions. Instead, the prices of goods and services must cover all the costs necessary to conduct the business, in other words, every good or service has included within its costs all direct costs plus the fair share of indirect costs. As for the time that workers in the economic unit spend on the necessary activities that perpetuate the operation of the economic unit, such as training and production development, and work development must be priced to make calculations of the time that "cannot be put in lists", meaning that the consumer has the right to determine which products and services he buys, but we leave the unit the economist is free to decide and manage its activities for indirect costs without consumer interference. The indirect costs (which are prepared in rates) also include expenses External seller such as professional development, product research, and peer-to-peer services do not be exclusively on a single row (indirectly internal) and indirect industrial costs at the level of the economic unit, such as internal support services and the management of the economic unit as a whole.

**Determinants of budget preparation on the basis of ABB activities**

The process of preparing the budget on the basis of activities ABB faces many limitations when applying them, which include the followingbased on (Awad and Al-Muaini, 2000) the activity changes during a short or seasonal period of time, which creates difficulty in application. When activities fluctuate seasonally (for example), their fixed components will have an equal influence on the budget and these activities will not provide an appropriate tool for oversight purposes. When leveling and allocating resources to support activities, there is definitely some objectivity.

The most important aspects of the difference between download rates based on activities and download rates on a traditional basis can be highlighted in the following: If we wanted to prepare download rates on the basis of activities, we will determine the centers of the cost of activities, the cost guides for each activity, and the indirect costs of that activity. Assuming that there are five activity cost centers, in this case, we will need five cost complexes and five cost directors, of which five are the loading rates as shown in Table (1). If we set the loading rates on a monetary basis, the rates will be prepared for the production cost centers only, or for one download rate as indicated in Table (2) or two rates of loading to be fixed and variable.

**Table (1) rates based on the ABC system**

| The complex | Cost oriented | Indirect costs | Amount of vector | Rate |
|---|---|---|---|---|
| 1 | Machine working hours | 13500 | 3000 | 4.5 |
| 2 | Production turnover number | 1850 | 4 | 462.5 |
| 3 | The number of engineering modification requests | 2000 | 10 | 200 |
| 4 | The amount of material transferred | 500 | 10000 | 0.05 |
| 5 | Direct business hours | 5400 | 10000 | 0.54 |

Source: Fakhz and Al-Dulaimi, (2002), industrial cost accounting, Part I, International House and the House of Culture Scientific Publishing and Distribution, Amman, p. 432, and adapted from the researcher.

**Table (2) Loading rates on the traditional basis**

| Production center | Industrial indirect costs | Base amount | Rate |
|---|---|---|---|
| A | 23250 | 3000 | 7.75 |

**Source:** Fakhz and Al-Dulaimi, (2002), industrial cost accounting, Part I, International House and the House of Culture Scientific Publishing and Distribution, Amman, p. 430, and adapted from the researcher**.**

**Requirements and general steps for applying modern methods ABB, ABC in Cost Accounting**

The application of modern methods, including ABB and ABC, requires the presence of some requirements that increase the chance of successful application and achieve the desired benefits and advantages, and so that the benefits derived from them are more than the costs of their application. Perhaps the most important of these requirements, which were identified by some as follows:

1. **Cost awareness:**

The term culture of economic unity refers to the rationality of employees and their intelligence, including their values, their functional goals and a strong job culture that clarifies values and goals and can be achieved through the adoption of values and concepts based on cooperative work with the participation of all members of the economic unit through teams working to suggest and make appropriate changes.

**2. Senior management commitment and support:**

Modern systems require sufficient time and resources to implement them, and these come from the support of senior management in material and moral terms, which represent the features of successful implementation.

**3. Spearhead (champion of change)**

One of the problems facing the application of modern methods is the failure to get the people who are influential in the economic unit (those with influence) who believe in the process of change because the accounting methods in any economic unit are similar to mathematical rules, in which people become accustomed to work on the basis of these rules and resist the addition of any Something they do not understand, and the hero of change is an individual who has a special effort to bring about change and has a high skill and has a strong impact on economic unity and also has the ability to persuade others.

**4. The change process:**

The meaning of the change becomes likely to be obtained if there is a definition of the new process, including scheduling specific activities, setting goals and detailing them well, and following up on the necessary elements of the change process.

**5. Continuing Education:**

The successful implementation of modern methods ABB and ABC require training of workers because the introduction of the principle of continuing education will lead to the practice of working in a transitional way that the worker performs in the same way as the previous generation (Awad and Al-Muaini, 2000; Madan Mohan and Prabhu, 2013).

**General steps for implementing ABC activities**

For the purpose of the design or operation of the ABC system in general and in any facility, whether industrial or service must follow a number of steps or stages of the design ABC system. Where the researcher agrees with the division of stages and steps into ten, but it must be pointed out here that the important thing is not the number of these steps or stages as much as it is important for the system to be integrated and achieve the desired goals from it. It should be noted that attention must be paid to training and educating the persons who will be entrusted with the implementation of the ABC system on the advantages and benefits of its application, taking into account the follow-up, evaluation, and analysis of the results of its application. Here is an explanation of these steps in some detail (Fakhz and Al-Dulaimi, 2002).

**First: Defining and defining appropriate activities:**

It is the primary stage in the system creation process and requires a review of the facility's technical and organizational maps, analysis of the basic and subsidiary activities and processes with a view to identifying and categorizing activities and preparing an activity plan or so-called activity model, where each core activity or homogeneous set of sub-activities is subject to one set of applied criteria, The preparation of the activity model facilitates the resource use planning process and contributes to improving the job process.

**Second: Dividing activities into activity centers:**

At this stage, the activities and processes required to manufacture the product are clear and detailed defined through the flow of process maps. In fact, there is an enormous amount of activities and operations performed for this purpose. The decision to group activities and consider them as activity centers by analyzing the relationship between the occurrence of activities (the causes of activities) and the achievement of costs, taking into account the cost-benefit factor (Sheikh et al. 2014). The activity center is defined as a part of the production process, the administration needs to report its cost independently, and the possibility of merging the activities depends on the extent of the difference between the company's products (Utterback and Abernathy 1975; Basariya and Ahmed, 2019).

**Third: Determine the main elements of the cost:**

Raw materials, parts purchased, purchased external services and similar direct costs on products are allocated directly without additional cost tracking analysis. However, with regard to the elements of indirect costs, it may be necessary to carry out a more detailed and detailed analysis of them than what is already in the records of the economic unit, and this is considered necessary to achieve two objectives:

1- Accuracy in predicting the cost of each component.

2- Achieving an adequate distribution of the amount of the cost component among the beneficiary cost centers.

**Fourth: Defining the relationships between activities and costs:**

After identifying activities and classifying them to activity centers and establishing the cost elements, it is necessary to determine the relationship between the activities and the different cost elements, i.e. determining the benefit of each activity from the cost element, where the real benefit is the determinant of allocating the cost elements to the activities.

**Fifth: Determining the cost guides:**

The stage of choosing cost guides is the most important stage of implementing the ABC system, considering that multiple and different cost guides are one of the most important features of the ABC system that distinguishes it from traditional cost systems, and it is also a link that links the cost to the activity and then to the cost goals. Therefore, care and caution must be exercised when Choosing cost directors (Spedding and Sun, 1999; Nambirajan and Prabhu, 2010).

**Sixth: Form a cost flow model:**
The stage of forming a model for cost flow is considered one of the basic and important stages in the framework of designing and implementing the cost system on the basis of activities. This stage requires accurate identification of components of indirect costs, and also specifying the types of cost centers to which the facility is divided, where it becomes possible to determine the cost flow form.
**Seventh: Choosing the appropriate methods to implement the system:**
The process of selecting means to implement the cost system on the basis of activity ABC is an important step in the framework of building this system, and the system designer must ensure that the largest possible number of means is available in order to choose the appropriate ones, taking into account that health is preferred over high costly accuracy. The presence of some common characteristics among a number of vectors of cost occurrence helps to suggest a single alternative to the occurrence of costs that can converge between all these vectors as one group.
**Eighth: Planning a Cost Compilation Form:**
Building cost based on activities according to the mentioned steps increases the volume of cost data and deepens its analytical function, and this is evident by preparing a cost flow model that consists of three levels related to cost elements and four other levels related to activity centers. Which appears to be difficult to set up manually or re-modify whenever needed. However, the use of modern electronic computers made the process of preparing and adjusting the model whenever the need arose for that.
**Ninth: Collect the necessary data to build a cost collection model:**
Good historical data may be available to help build a cost compilation model, but it may be evident that no such data is available. Therefore, personal interviews and the estimation process should be resorted to using staff with knowledge and experience.
The necessary and necessary information is collected on each level of cost flow and preparation of schedules or a worksheet for submission to the cost collection form.
**Tenth: Building a Cost Compilation Model:**
The cost collection model is built according to the previous levels by computer Online, where data is collected on a set of computer pages and in a possible way introducing changes without much effort. Data on salaries, wages, in-kind benefits, and specific special costs are entered until they are completed, after which the model is provided with the appropriate allocation bases, then data on the levels from the fourth to the eighth are followed, where the cost elements in each level are collected and allocated to cost centers, and then its full cost shall be borne by the cost targets. The tables that relate to this part of the form are called cost allocation tables, after which tables are prepared that summarize the total centers' costs and loading rates.

**General steps for budgeting based on ABB activities**
The book differed in the number of steps for preparing a budget based on activities ABB, Drury identified five main stages of budget preparation on the basis of activities as follows: (Drury et al. 1993)
1- Estimate production and sales volume by individual products and consumers.
2- Estimate the demand for the activities of the economic unit.
3- Determining the resources required to carry out the activities of the economic unit.
4- Estimating the quantity required for each supplier, which must be prepared to meet the demand.

5- Take action to normalize the resource capacity to be in line with the expected supply or equipment.

While another believes that the budget can be prepared on the basis of activities as follows:

1- Determine activities and their cost guides.

2- Determine the costs of activities.

3- Determine the direction of the actual activity costs.

4- Building a budget for the activity.

The following is an explanation of the steps to prepare a budget based on activities: (Drury et al. 1993; Dixit et al. 2019)

**First: Estimate production and volume of sales by individual products and consumers**

The first stage is similar to the traditional budget preparation, as production details and sales volumes in the budget for products and consumers will be within the budgets for sales and production.

**Second: Estimating the demand for the activities of the economic unit**

The budget on the basis of activities is for activities that add value, and on the basis of using the appropriate activity cost guide, then it is necessary to determine the activities for which the budget is prepared according to the appropriate cost guide, and the cost system data is based on activities ABC in determining these activities in light of the needs of the economic unit To do its effectiveness.

**Third: Defining the resources required to carry out the activities of the economic unit**

The third stage is to determine the resources required to accomplish the required quantity of activity guides, especially that estimates are required for each type of resource, and the quantities required to meet the required amount of activities. For the purposes of assessing performance efficiency, it is preferable to use activity time measures (direct activity cost directives) on the basis of which activity inputs are measured by converting The non-temporal metrics (directors of indirect costs of the activity) on the basis of which the outputs are measured according to the following formula:

The time required to perform the transport activity = Time required to move each batch x number of batches Under this equation, the non-time cost of the activity (number of batches) was converted into a time-cost-oriented activity cost (time needed for the activity) and this applies to other non-time cost directors such as the number of designs and the number of complete production units.

**Fourth: Estimating the quantity required for each supplier, which must be prepared to meet the demand**

Then the required resources (derived from the third step) are converted into an estimate of the total resources that must be equipped for each type of resource used by the activity. The amount of resources provided depends on resource cost behavior. For flexible resources, where the supply can be adjusted exactly to meet demand, such as direct materials and energy costs, the number of resources equipped will be the same as the quantity required. As for other resources such as equipment, the resources will tend to be fixed and binding over a very wide chain of size in relation to the activity. And as long as the demand is less than the energy supplied by the binding resource, there will be no demand for additional spending.

**Fifth: Take action to level the resource capacity to be in line with the expected supply or equipment**

The last stage is to compare the estimate of the number of resources required to be prepared for each resource with the number of resources currently planned. If the estimated supply of the resource exceeds the current capacity, then additional spending must be authorized

within the budget process in order to acquire additional resources and vice versa. If the demand for resources is less than the expected supply then it results from the budget preparation process. The administration takes action, either to transfer those resources to another location or to reduce them because they are no longer are required.

**Conclusions**

The ABC system divides the economic units into sub-activities and analyzes them and knows how they consume costs and the extent of their contribution to the production process, which leads to a reduction in costs by knowing which activities add value or do not add value to production and dispense with activities that do not add value. The ABC system of cost-based activities assists management in making appropriate management decisions based on more realistic costs, which are useful in various fields such as those related to pricing. The primary goal of preparing the budget on the basis of activities ABB is to authorize the supply of those resources that are required to meet the production and volume of sales in the budget and thus the optimal use of resources. The analysis of elastic budget deviations based on activities and each activity is more the depth of the traditional analysis as it analyzes the deviations of each activity separately on the basis of its cost orientation. By comparing a cost system based on ABC activities and the conventional cost system applied in the textile factory in Mosul, it was found that the ABC system is more accurate in measuring and determining the production cost and the unit of products produced from the traditional cost system, and this, in turn, is reflected in the cost accounting objectives (planning) Supervision and decision-making) given the more accurate and objective data provided by the ABC system for plant management.

**Recommendations**

Based on the theoretical and practical study, and in light of the above mentioned conclusions, the following can be recommended are made. Working on studying and evaluating the cost system currently approved by the laboratory, the research sample, and making the necessary adjustments and changes, according to the scientific and practical foundations, appropriate and appropriate to the activities of the economic unit, so that in the future it can be developed and applied modern methods ABB, ABC. Work to develop the accounting cadres supervising the operation of the cost system in the industrial units of the research sample, by preparing specialized courses in the field of modern methods of cost accounting, using the assistance of specialized university professors, consulting offices and expert homes to increase the accounting awareness of cost accountants. Supporting the responsible senior management in the laboratory, the research sample, applying the modern methods ABB and ABC in cost accounting, both financially and morally, in order to keep abreast of the modern developments taking place in the developed world. The need for management to recognize the importance of the elements of indirect costs and the impact of their allocation on the products in determining more accurate costs for the products and thus to take more efficient and effective management decisions. Utilizing the ABC activities data system in preparing the budget based on ABB activities in the units that apply these methods.

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