***Top down or bottom up budgeting?***

Are you simply allocated a budget, or are you involved in deciding how much budget you need? Top down budgeting is when “the centre” (the directors, supported by the Finance department) allocate budgets to budget holders. Bottom up budgeting is when budgetholders outline the budget they need for the coming year. Both approaches have their strengths and weaknesses.

**Top down budgeting**

This centrally driven process is designed to ensure that the business lives within its income. Once sales have been forecast, budgets are allocated. It’s a quick, simple and straightforward process, that leaves the centre firmly in control.

On the other hand, budgets are allocated in an arbitrary way, with little connection between the amount of allocated budget and the actual needs of the budgetholder.

**Bottom up budgeting**

Here budgetholders begin the process, and calculate how much budget they need to achieve their objectives. Budget bids will then be totalled, and compared to forecast sales. This usually indicates a catastrophic loss, resulting in further rounds of tighter budget bids.

So it’s a slower process. Human nature dictates that most budgetholders will ask for a comfortable budget allocation rather than a challenging budget, so it may take several iterations before the process throws up an acceptable result and real value for money. This is exacerbated by the sense of “I’d better ask for too much, because I’ll only be told to reduce it later.” But the real strength of bottom up budgeting is that the budget process is linked to the budgetholders’ objectives. How much people are spending is linked to what they’re doing.

**The bottom line: which approach is right?**

Both approaches are right!

The bottom line for the business is that it must be profitable. It can’t afford to allocate more in budgets than its income.

The bottom line for the budgetholder is that they must have enough budget to finance the resources they need to deliver their objectives.

That’s why many businesses adopt a bottom up budgeting process, that usually involves several rounds. It will only be successful when:

* the centre is happy that the business will be profitable and living within its income
* the budgetholders understand the link between their objectives and their budget, and are happy that they can deliver both