Management Accounting

PRACTICAL CLASS 18

Illustration by Ana Seixas

Budgeting

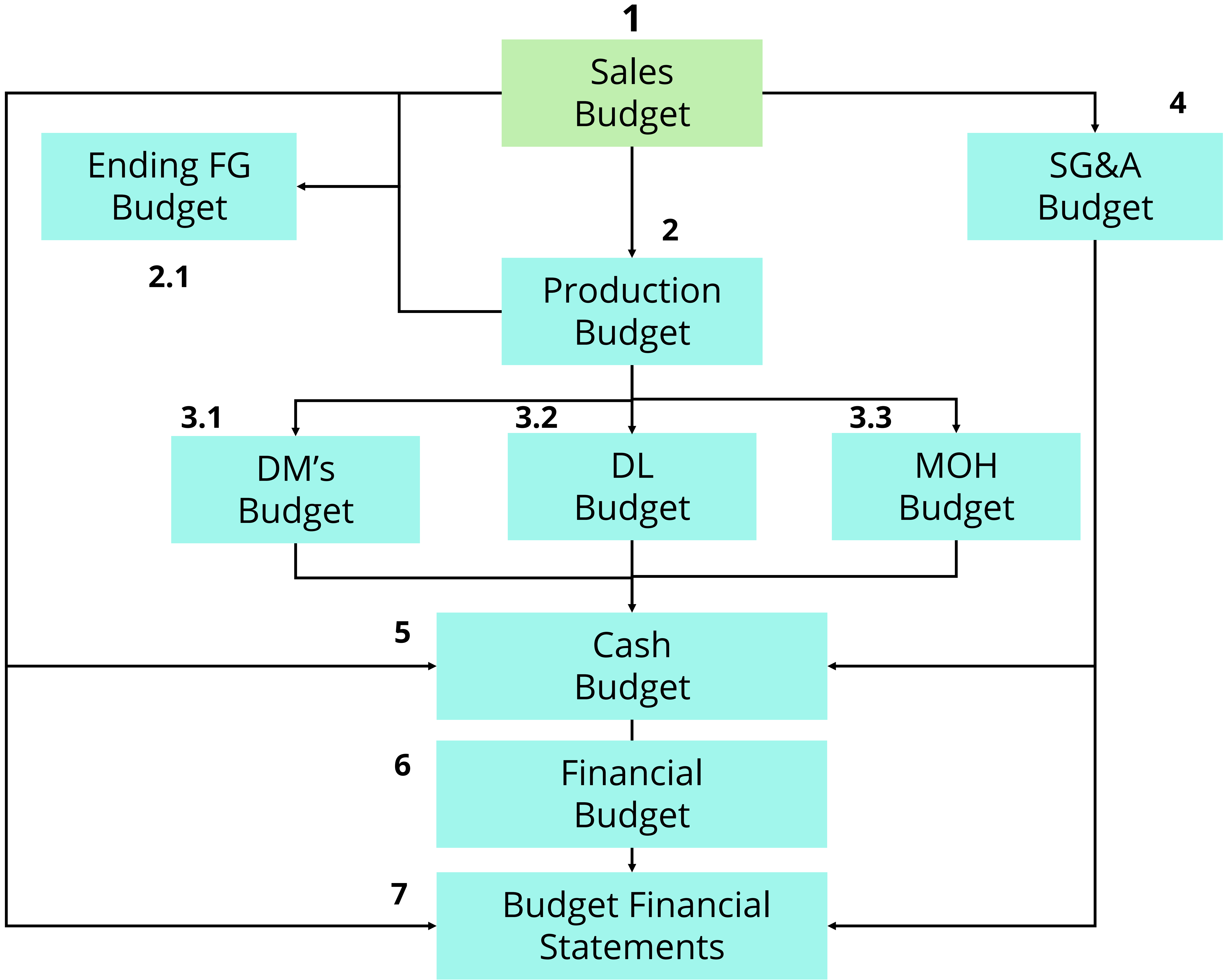
UNFOLDING A LONG-TERM STRATEGY IN A SHORT-TERM PLAN

Planning	What do we want to achieve, where and how?
Coordination	Ensure that the company is fully oriented towards the same goal/ conflict resolution
Communication	Everyone knows what is the plan
Motivation	Everyone has a target, to which rewards can be linked
Control	You can’t understand how far you deviate from the plan unless you have one to begin with ☺
Performance Evaluation	Budgets provide a benchmark to beat ☺

The Master Budget

THE BIG THING

- A detailed and comprehensive planning document for the entire organization
- It incorporates the three Budgeted Financial Statements



Sales & Inventory

SOME GENERAL GUIDANCE

Sales Budget *(regardless of payment)*
+ Sales (Units * Selling Price)
+ VAT (VAT rate * Sales)
= Sales + VAT

DM Purchases Budget (regardless of payment)
+ Purchases (Units * Purchase Price)
+ VAT (VAT rate * Purchases)
= Purchases + VAT

Budgeted FG Inventories (# or €)
+ Opening Inventory
+ Production (COGM)
- Sales (COGS)
= Closing Inventory of FG

DM Budget
+ Opening Inventory
+ Purchases
- Consumption (DM)
= Closing Inventory of FG

Production & Cash

SOME GENERAL GUIDANCE

COGM Budget
+ DM’s
+ Variable Conversion Costs
+ MFC *****(Depends on the Costing System)
= COGM

Operating Cash Balance = Total Receipts - Payments

Operating Cash Budget
Cash Inflows
+ Sales Collection
= Total Receipts
Cash Outflows
+ Purchases DM
+ VAT Payable
+ Variable Costs
+ Fixed Costs
+ Other Payments
= Total Payments
= Operating Cash Balance

Financial Budget

SOME GENERAL GUIDANCE

Sources of Funds
+ Opening Cash
+ Positive Cash Balance
+ Loans (ST & LT)
+ Interest Received on Financial Investment
+ Sale of Financial Investments
+ Sale of Equipment
= Total Sources of Funds

Uses of Funds
+ Closing Cash
+ Negative Cash Balance
+ Reimbursement of Loans (ST & LT)
+ Financial Investments
+ Interest Payments
+ Purchase of Equipment
= Total Uses of Funds

Total Sources of Funds = Total Uses of Funds

Budgeted P&L

SOME GENERAL GUIDANCE

- No VAT
- Financial Costs = Interest Expense
- UROH = Depends on the Costing System ;)
- Regardless of Payment

P&L
+ Sales
- COGS
= Gross Profit
- UROH
- Selling Costs
- Administrative Costs
= Operating Profit
- Financial Costs
+ Financial Revenues
= Profit Before Taxes

Budgeted Balance Sheet

SOME GENERAL GUIDANCE

Assets
+ Plant, Property & Equipment – Depreciation Year N
+ Inventories (DM + FG + WIP)
+ Accounts Receivable
+ Financial Investments
+ Interest Receivable (Financial Investments)
+ Cash & Cash Equivalents

ASSETS = EQUITY + LIABILITIES

Equity
+ Equity N-1
+ Profit Before Taxes N

Liabilities
+ Loans (ST & LT)
+ Accounts Payable to Suppliers
+ Other Accounts Payable (S&A Expenses)
+ Accounts Payable to State (VAT)
+ Interest Payable

Budgeting Tips

TIPS YOU MAY FIND USEFUL FOR BUDGETING EXERCISES

Be structured: (sometimes) it's better to do the smaller budgets as they provide info needed to do cash, financial and budgeted financial statements.

Don’t forget Accrual Based Accounting**: Revenues and Expenses are recorded in the periods they are generated (this is very important for the Budgeted P&L): Pay Attention to Interests!**

Don’t forget the reasoning for **Financial Budget**: **If sources > uses:** you reimburse your loan (if you have one) or you invest (this depends on the financial information given in the exercise); **If sources < uses**: ask for a loan!

VAT is **NOT a Revenue nor an Expense** (thus, it is not present in P&L~~)~~, but something you collect from customers, pay to suppliers, and deliver the difference to the State, thus **affecting Cash Balance (Flows).**

In the **Cash Budget,** while accounting for expenses**,** consider only cash expenses (**do not deduct depreciation**!)

While doing the **budgeted balance sheet**, do not forget to:

- Add Net Income to Equity!
- Subtract Depreciation from Tangible Assets!
- Consider everything payable and receivable (interest, VAT, suppliers, clients…)!

Exercise 55

THE INDUSTREX DA BEIRA LITORAL COMPANY