CHAPTER LEARNING OBJECTIVES:

MAJOR:
- Calculate selected budgeted amounts based upon given data.
- Be familiar with various budgets and master budget.

NOT IMPORTANT:
- Memorizing all budget formats as shown in text.
- Memorizing the exact order of budget preparation.

A BUDGET is a formal (detailed and in writing) plan for the future expressed in quantitative terms.

Good budgeting includes Planning and Control.
PLANNING is developing future objectives and formulating the steps necessary to achieve those objectives. I.e., PLAN
CONTROL is the means taken to ensure the organization achieves the objectives. I.e., DO & REVIEW

Benefit of budgeting is that it coordinates the activities of the organization. In effect, everyone working together for a common goal.

RESPONSIBILITY ACCOUNTING is holding accountable those managers who have the ability to control costs. I.e., evaluating managers based upon their area of control (responsibility).

PERPETUAL BUDGET is usually 12 months, adding on one month as one month drops off.

SELF IMPOSED (PARTICIPATIVE) BUDGET is prepared with the cooperation and participation of all levels of management.

MANUFACTURING FOH BUDGET is not a cash budget (because it would include depreciation).

DEPRECIATION, amortization and depletion, and losses are not cash expenses (outflow), nor is a gain a cash inflow.

Steps in budgeting:
1. Sales forecast comes before any budgeting.
2. Sales budget needs to be prepared first.
3. Production budget will depend upon sales budget and desired beginning and ending inventory levels.
4. Other budgets will follow.
5. Budgeted financial statements would come last or near the last.

See the next page for a summary description of various budgets and the approximate order of preparation. Familiarity, not memorization, of the basic steps in formulating a master budget is required.

When it comes to budget calculations, it is nothing more than a "written-out math problem". Use your common sense, knowledge of basic addition, subtraction, multiplication and division, and knowledge of basic accounting terminology and concepts to solve the problem (prepare the budget). Each budget problem will describe what mathematical calculations are necessary to solve it.
Basic Steps In Formulating A Master Budget

1. Prepare a sales forecast, generally based on a combination of estimates by the sales staff, statistical analysis, and group executive judgment.

2. Prepare a production budget based on the sales forecast (step 1).
   Units to be produced = Budgeted sales + Desired ending inventory - Beginning inventory.

3. Prepare a schedule of material usage and purchases.
   a. Usage will depend on the level of production as budgeted (step 2).
   b. Purchases in units = Usage + Desired ending material inventory - Beginning material inventory.

4. Prepare a schedule of direct labor costs, based on production level (step 2), estimated labor rates, and labor methods.

5. Prepare a schedule of manufacturing overhead costs. This schedule consists of two parts:
   a. Fixed overhead (remains stable over a wide production range).
   b. Variable overhead (determined by the production budget (step 2) and the per unit budgeted costs).

6. Prepare a schedule of desired ending inventory levels, to be used for the construction of budgeted financial statements.

7. Prepare a cost of goods sold budget, using the information gathered in 3 through 6, above.

8. Prepare a budget of selling, administrative, and other expenses, usually determined by group executive judgment and statistical analyses.

9. Prepare a cash budget, taking into consideration the effects on cash position of the level of sales and related collections of cash, and on production and the related disbursements of cash.
   a. Beginning cash + cash receipts = Total cash available before financing.
   b. Cash disbursements = Purchases of materials + Salaries and wages + other cash outlays + acquisition of fixed assets + Investments. (Note that non-cash expenses such as depreciation are not included.) Future anticipated dividend payments would normally be included in the cash budget.
   c. Financing requirements include repayments of the obligations, interest expense, and other investments that may be planned.

10. Prepare a budgeted income statement. (Note: an income statement would include depreciation and other non-cash revenues and expenses.)

11. Prepare a budgeted balance sheet, using the information gathered for other budgets. For example, accounts receivable equals budgeted sales, plus beginning accounts receivable balance, less estimated cash receipts.

12. Prepare a capital expenditures budget. This should take into account the facilities, equipment, etc, required to achieve the budgeted level of production, long-range expansion plans, and the cash available for capital expenditures (from the cash budget). This budget could be completed prior to the income statement and balance sheet.