

MASTER BUDGET

- The master budget consists of a number of budgets
- These include sales, production, direct materials, direct labor, manufacturing overhead, selling and administrative expenses, cash receipts and disbursements, and budgeted financial statements
- The master budget is a collection of smaller budgets that leads to pro-forma (budgeted) financial statements
- The first component of the master budget is the functional budgets. In addition the master budget contains the cash budget, budgeted income statement and budgeted balance sheet
- Each of the budgets impacts the company's cash position, income statement, and balance sheet. The sales budget is the key to the entire master budgeting process, since most other master budget components depend on the level of sales. The pro-forma income statement and balance sheet are prepared from numbers contained in the various components of the other budgets

18.1 Cash Budget

- Cash budget is a detailed plan showing how cash resources will be acquired and used over some specific time period
- Cash budget is composed of three major sections
 1. The receipts section
 2. The disbursements section
 3. The cash excess or deficiency section

18.1.1 The receipts section

- ✕ The cash receipts section consists of a listing of all of the cash inflows, except for financing, expected during the budgeting period. Generally, the major source of receipts will be from sales

Example #18.1: Naeem Corporation analyzed its payments from customers, it found that 30% of the invoiced amounts were paid in the same month as the work was done and the other 70% were paid in the following month. Revenue information for selected months is presented below:

| <i>Month</i> | <i>Revenue</i> | <i>Month</i> | <i>Revenue</i> |
|---------------|----------------|---------------|----------------|
| November 2011 | Rs. 85,000 | February 2012 | 87,000 |
| December 2011 | 90,000 | March 2012 | 69,000 |
| January 2012 | 92,000 | April 2012 | 83,000 |

Calculate the monthly cash receipts for January, February, and March of 2012

Solution:

| Description | January | February | March |
|--------------|-------------------|-------------------|-------------------|
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| Total | Rs. 90,600 | Rs. 90,500 | Rs. 81,600 |

Example #18.2: All of Ali and Ahmed’s sales are on account. In the past, 15% of the amounts charged have been paid in the same month as the sale, 60% were paid in the following month, and the rest were paid in the second month following the sale. Sales for selected months are given below:

| <i>Month</i> | <i>Revenue</i> | <i>Month</i> | <i>Revenue</i> |
|---------------|----------------|--------------|----------------|
| November 2010 | Rs. 580,000 | March 2011 | 750,000 |
| December 2010 | 600,000 | April 2011 | 725,000 |
| January 2011 | 550,000 | May 2011 | 700,000 |
| February 2011 | 650,000 | | |

Prepare the cash receipts budget for the first three months of 2011

Solution:

| Description | January | February | March |
|--------------------|--------------------|--------------------|--------------------|
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| Total | Rs. 587,500 | Rs. 577,500 | Rs. 640,000 |

18.1.2 The disbursements section

- The disbursement section consists of all cash payment that is planned for the budgeted period
- These payments will include raw materials purchases, direct labor payments, manufacturing overhead costs, and so on as contained in their respective budgets
- In addition, other cash disbursements such as equipment purchase, dividends, and other cash withdrawals by owners are listed

Example #18.3: Anees Fida Company pays for 40% of its inventory purchases in the month of the purchase and the remainder in the following month. The company’s inventory purchases totaled Rs. 850,000 in October, Rs. 980,000 in November, and Rs. 720,000 in December. The company also paid for new equipment with a total cost of Rs. 520,000 in November and made a tax payment of Rs. 130,000 in December. Salaries and wages were paid as follows: Rs. 310,000 in October, Rs. 300,000 in November and Rs. 295,000 in December.

Determine the firm’s cash disbursements for November and December

Solution:

| Description | November | December |
|--------------|----------------------|----------------------|
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| Total | Rs. 1,722,000 | Rs. 1,301,000 |

Example #18.4: Pakistan Company has budgeted the following information for 2011:

| | <u>May</u> | <u>June</u> | <u>July</u> |
|--------------------|-------------|-------------|-------------|
| Budgeted purchases | Rs. 104,000 | Rs. 110,000 | Rs. 102,000 |

- Cost of goods sold is 40% of sales. Accounts payable is used only for inventory acquisitions
- Company purchases and pays for merchandise 60% in the month of acquisition and 40% in the following month
- Selling and administrative expenses are budgeted at Rs. 30,000 for May and are expected to increase 5% per month. They are paid during the month of acquisition. In addition, budgeted depreciation is Rs. 10,000 per month
- Income taxes are Rs. 38,400 for July and are paid in the month incurred

Instructions: Compute the amount of budgeted cash disbursements for July.

Solution:

| Description | July |
|--------------|--------------------|
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| | |
| | |
| Total | Rs. 176,675 |

18.1.3 The cash excess or deficiency section

- ♣ This section is result of above two sections
- ♣ If receipts is higher than disbursement than result is cash excess
- ♣ If receipts is lower than disbursement than result is cash deficiency

Example #18.5: Waleed, Inc. has budgeted sales revenues as follows for 2011:

| | <u>June</u> | <u>July</u> | <u>August</u> |
|--------------------|---------------------------|---------------------------|---------------------------|
| Credit sales | Rs. 135,000 | Rs. 125,000 | Rs. 90,000 |
| Cash sales | <u>90,000</u> | <u>255,000</u> | <u>195,000</u> |
| Total sales | <u>Rs. 225,000</u> | <u>Rs. 380,000</u> | <u>Rs. 285,000</u> |

Past experience indicates that 60% of the credit sales will be collected in the month of sale and the remaining 40% will be collected in the following month. Purchases of inventory are all on credit and 50% are paid in the month of purchase and 50% in the month following purchase. Budgeted inventory purchases are:

| | |
|--------|-------------|
| June | Rs. 300,000 |
| July | 240,000 |
| August | 105,000 |

Other cash disbursements budgeted: (a) Selling and administrative expenses of Rs. 48,000 each month, (b) Dividends of Rs. 103,000 will be paid in July, and (c) Purchase of equipment in August for Rs. 30,000 cash.

The company wishes to maintain a minimum cash balance of Rs. 50,000 at the end of each month. The company borrows money from the bank at 6% interest if necessary to maintain the minimum cash balance. Borrowed money is repaid in months when there is an excess cash balance. The beginning cash balance on July 1 was Rs. 50,000. Assume that borrowed money in this case is for one month.

Instructions

Prepare a cash budget for the months of July and August 2011

Solution:

Waleed, Inc.

Cash Budget

For month of July and August, 2011

| Description | July | August |
|----------------------------|----------------|----------------|
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| | | |
| | | |
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| | | |
| Total Cash Receipts | 434,000 | 349,000 |

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|---------------------------------|------------------|------------------|
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| Cash Disbursements: | | |
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| Total Cash Disbursements | (421,000) | (250,500) |
| | | |
| | | |
| Ending Cash Balance | 50,000 | 61,315 |

Example #18.6: Cooper Company has budgeted activity for January, 2011 using the following data:

| Description | Amount |
|--|------------|
| Cash sales | Rs. 25,000 |
| Credit sales (60% collected in month of sale) | 380,000 |
| Selling and administrative costs (including depreciation) | 50,000 |
| Depreciation expense | 5,000 |
| Merchandise Inventory, January 1 | 21,000 |
| Merchandise Inventory, January 31 | 20,000 |
| Beginning cash balance | 3,000 |
| Minimum cash balance required | 2,500 |
| Cost of goods sold is 55% of Cooper's selling price | |
| All purchases are paid in cash | |
| Selling and administrative costs are paid in month of purchase | |

Required: Prepare a cash budget for January

