Management Accounting
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Lecture 22: Master Budget: A Mini Case 2

Welcome students. So we are in the process of preparing the cash budget for this quarter and in the previous class we prepared the budget for month of January and we have already means put the particulars, all kind of the particulars here in this statement.

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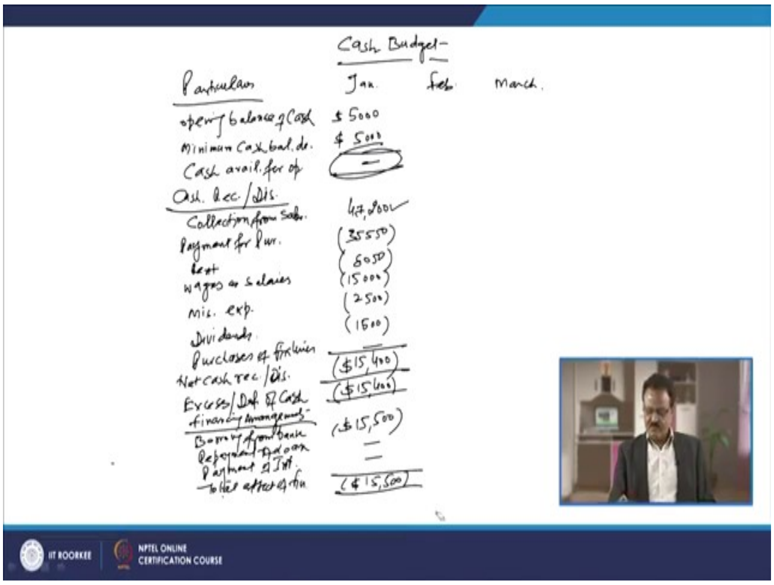

So, all these particulars they remain same for the month of February also for the month of March also. We will have to calculate the closing balance for the because we started with opening balance for the month of January which was the closing balance for the month of December so that became the opening balance for the month of January and then after that we had to calculate the closing balance for the month of January after adjusting all the say inflows and outflows or say receipts and payments.

So we saw that our opening balance first 5,000 dollars and we have to keep 5,000 dollars as the minimum cash, so cash available for the operation was nil. Then we went for the collections which we found out here 47,200 dollars and then subtracted all expenses so we had a negative balance of how much 15,400 dollars and then we found out that finally this is the deficit of the cash, means we are paying more by this amount of 15,400, we have receive less amount from the collection of sales so finally we are in the state of deficit for the 15,400.

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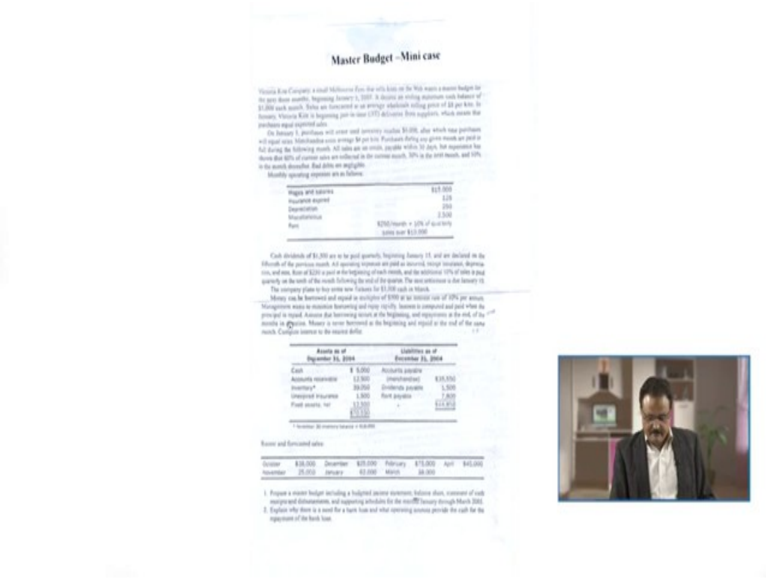

So we went for the financing arrangements and the condition there was, in the financing arrangements condition in the cases that we have to burn the multiples of 500. It is given here in the games that parents will be at there is a money can we borrowed and repaid in the multiples of 500 dollars at an interest rate of 10 percent so that condition we have to follow.

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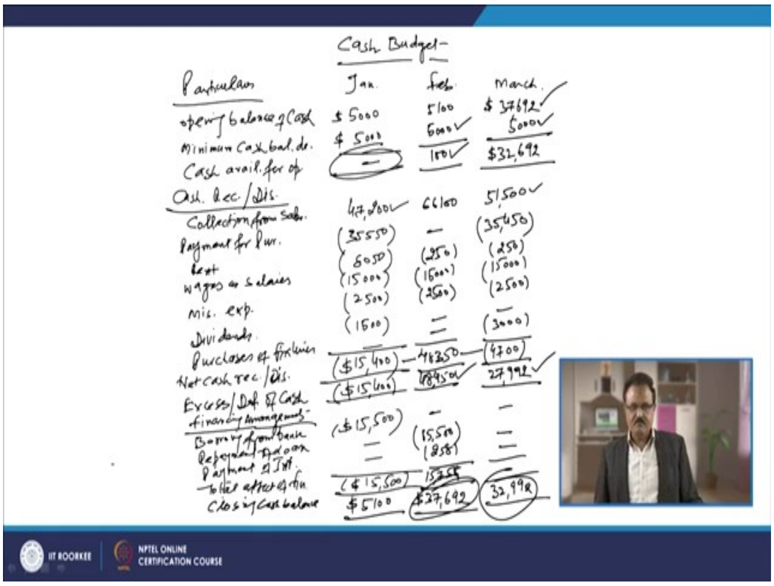

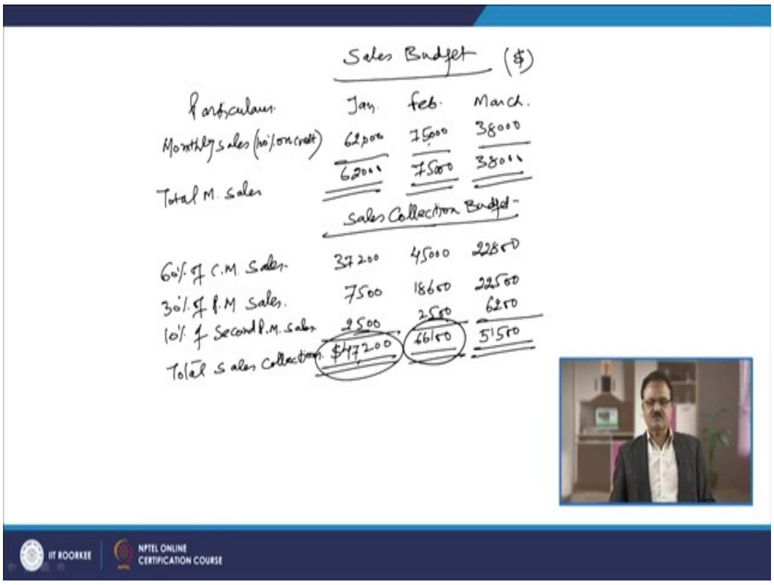

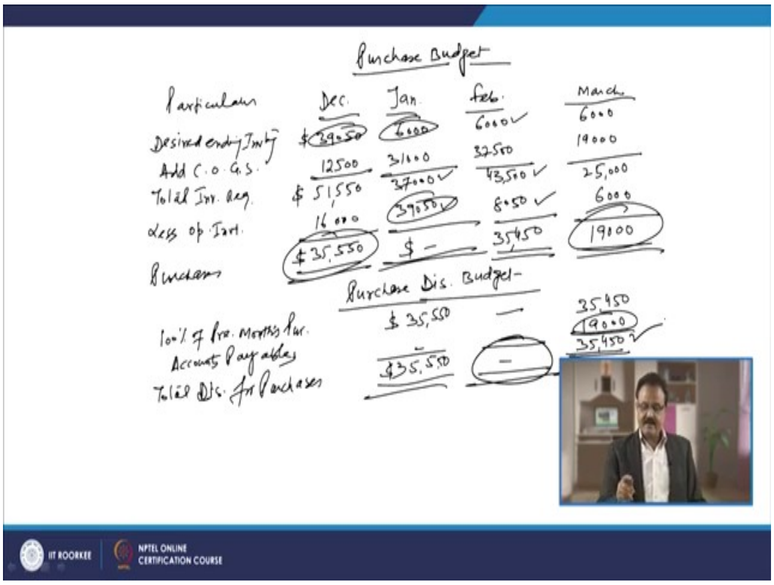

So you cannot borrow from the bank that the amount of deficit which is 15,400 but have to borrow in the multiples of 500 so we should here that is we have shown here that is the borrowing from the bank is 15,500 there is actual requirement is 15,400 so we had to go for this amount of the borrowing. So, when we borrowed 15,400 our requirement is, when we borrowed 15,500 our requirement is 15400 so it means now we are left with the balance of cash and that balance of the cash is how much that is the, we are left with how much.

This amount is 100 is left here and how much is the closing balance, minimum cash balance reside is 5,000. So, what is a closing balance of the cash, closing cash balance is 5,100 dollars. This is the closing balance of the cash. 5000 we have kept as the minimum cash balance is that that is a safety stock and 100 is left from the borrowing from the bank because we borrowed in the multiple of 5 that is 15,500. Actually we required 15,400, so 100 is left from this borrowing.

5000 is already there with us as a safety stock that is a minimum cash balance desired. So, it means now the closing cash balance is how much, 5,100 dollars, right. Now, this closing cash balance for the month of January will become the opening balance of the cash for the month of February. So, it means this is 5,100, minimum cash balance desired is how much, 5,000, right, so how much is the cash available for the operations, for the month of February it is 100 dollars.

This amount is 100 dollars and now we will go back to the collection schedule, sales collection schedule and in the sales collection schedule you will find that how much collections we are doing for the month of February 66,100; 66,100 is the collection, sales collection is that is this is the amount, 66,100 for the month of February we are collecting from the sales. So this amount will come here and now we will go for the payment schedule.

And if you talk about the payment schedule here that again from the say purchased disbursement budget plus other operating expenses directly to be taken from the case so we will have to put all the expenses here, and bring all those expenses or maybe the disbursements of the cash here so you will find that if you go back in the purchase disbursement statement, you will find here that what we are going to purchase disbursement budget.

So we have paid for or we had to pay 35,550 dollars in the month of January which you put in the payments column, first payment in the payments column of the disbursements column but in the month of February we have nothing to pay because no purchase was made in the month of January so no payment has to be made in the month of February. So, in this case this amount will be how much this will be payment for the purchases nil, so we are not going to pay anything because no purchasing happened done in the month of January so no payment will be made in the month of February, so nothing is due on account of the payment for the raw material.

Now, the rent, now the rent is only the regular rent of how much 215 dollars because this was that previous quarter's rent, so it was a 10 percent of more than 10,000 of the quarterly sales that amount worked out as the 7,800 plus 250 be added, so it became 8,050 but nothing of the sort is here in case of the month of February, only the amount is how much 250 dollars is going to be paid for this. So, this is the first payment we are going to make in the month of February and then we talk about the wages and salaries.

So wages and salaries are how much again 15,000 dollars and miscellaneous expenses are same, this amount is going to remain the same so this is the miscellaneous expenses and dividends, no dividends had to paid now in this quarter, this dividend of 1500 was paid for the previous quarter which was due on the 15th of January. So, we have already paid it and not this quarter's dividend will become due on the 15th of April so we are not preparing the cash budget for the 15th of month April so we will not put any kind of dividend so no dividend is going to be paid now, so no payment for that.

So, now finally you have to balance it and while balancing it a similarly fixtures payments are not in the month of February so it means finally our total payment is going to be how much. This is also going to be no payment no dividend no fixtures. Fixtures payment will be once only in the month of March. So when will go to the month of March will see there right. Now, but we have to do is, here is that is the, we will have to take this amount and we have to balance this.

So, if we balance this receipts and payments figure you come out with net cash received oblique disburse. What we have written net cash received/ disburse, now what is this 66,100 is collections and payments is very few only that is how much 15,500. So, we are left with this total amount of, this amount is that is no sorry, this payment is going to be how much, 17,750 this payment we have to make and what is our collection that is collection is 66,100.

The total collection is going to be 66,100 so finally we are going to have the net balance of something like 48,000 in the net balance of 48,350.What is the total amount that is 17,750 are the payments total, that is 250, 15,000 plus 2,500 this works out as 17,750 and our collections are 66,100 so what is the net difference, 48,350 dollars are left with us. Now, in excess or deficit of the cash is how much now, we have this much of the cash of 100 dollars which is available for the operations and now in this month of February we have the excess of the cash that is why 48,350.

So, finally, total excess of the cash will be how much 48,450, this is the total amount of 48,450 we have taken here. So, now this surplus have calculated, this excess of the cash we have calculated, and now we will talk about the borrowing or the financing arrangement or the borrowing from the bank or means making the repayment to the bank because as I told you that if there is a shortfall of the cash you can borrow from the bank and if there is a surplus of the cash in any of the month then we can make use of that surplus for the repayment of the loan which we have borrowed in the previous month.

So in this case we will have to make the repayment back to the back so that means borrowing for the bank is nil. We are not borrowing any amount from the bank in this case. So for now we have a left with this amount of surplus that is 48,450 and then we have borrowed how much 15,500. So the entire amount which we have borrowed in the previous month can be paid back to the bank in this case repayment of the loan, how much is the repayment of loan of 15,500.

This is the repayment of the loan and at the same time we have to work the interest on this amount and if you work out the interest on this amount at the rate of 10 percent on this borrowing the 15,500 at the rate of 10 percent per annum for a period of how many 2 months, we borrowed in the beginning of January and we are repaying it back at the end of the February so the total interest works out as how much 258 dollars. So this also has to be paid. So total payments are going to be, total effect of financing here going to be how much that is 15,758 we are going to pay back to the bank.

So we had borrowed 15,500 and we are returning that after 2 months and we are returning that with the interest of that is 258 which work out at the rate of 10 percent for the period of 2 months. So the total amount which we are returning back to the bank as a total effect of financing we have shown or the returning the loan we have shown is the 15,758 so closing cash balance is how much we are left with, closing cash balance we are left with is, that this amount of 48,450 minus 15758.

So, we are left with some about here 48,450 minus 15,758 this is the one amount plus the minimum cash balance desired of how much that is of 5000. So this plus this difference of 48,450 minus 15,758 this amount works out as how much, this is the closing balance of the cash dollar 37,692 this amount is now available with us at the surplus because we had this minimum cash balance of 5,000, we got excess here of the 48,450, means after adjusting, adding up that or say cash available for the operations that is 100 dollars.

And from this part 48,450 we use the amount of 15,758 to repay back the, repay the loan and finally we are left with some amount here plus this amount to the closing cash balance of the cash is 37,692. So the closing cash balance for the month of February is going to be the opening balance for the month of March and this is going to be how much, same amount 37,692 this is the opening balance for the month of March. Now, again same thing minimum cash balance desired in how much 5000.

Now the cash available for the operations in so much 32,692 dollars this is the cash available for operation, this is cash available for operations so this is 32,692 is there and now we will have to again start the adding up all the figures here. So, first is the in case of the cash received/disbursed first is a collection from sales, how much is a correction from for from sale in the month of March election from the sale for the month of March 51,500. So let us put this figure here 51,500.

Now payment for purchases, are we going to pay for the purchases yes we are going to pay for the purchase is here that is how much that is 35,450 which we have to pay in the month of March, so this amount will come out as, first payment we are going to make here is 35,450 this is a first payment and payment for what, it is a payment for purchases, again then other items are normal, 250 dollars for rent and then is the wages and salary. How much it is 15,000 wages and salaries is 15,000 and how much is other, miscellaneous expenses are again 2,500 these are miscellaneous expenses we are going to pay.

Dividend as I told you, no dividend is due till the month of March, it will be due in the month of April and one more payment we are going to make here is acquisition of fixtures and that is worth rupees, how much that acquisition of fixtures is given here something? The company plans to buy some new fixtures for 3,000 dollars in cash in the month of March right so that we are going to purchase know the fixture to pay for that this. So, this we are going to pay this in cash, so these are the total disbursement.

This is a collection amount 51,500 the minimum cash balance we have kept. So that how much is not available with us is 56,500 dollars and sum total of these expenses or the disbursements will be put here, this is coming after how much difference, the difference will come up here is 35,451; 250 is another, 15,000 is another and 2,500 plus 3000 we are going to pay so you can finally find out what is the excess, say deficit of the cash. I think again in the state of deficit here, so it means we will have to find out here that is from this particular situation if you look at.

How much is the elections 51,500, payments are more than that. So, if you look at the balance that is the net cash received oblique disbursed is how much we are running into the total deficit of 4700 dollars. This is the deficit we have got a negative figure here because our collections are less our payments are more. So, if you compare this part only then you will find the net balance, is net cash received oblique disbursed 4,700, right. But, now nothing to worry about we have sufficient cash available for operation say that is 32,692 and minimum cash balance desired here is that is 5000.

So, if you calculate the total balance available here after adjusting for everything then finally we will be able to find out that our net balance is going to be very good, very positive balance we have with us. It means if you calculate this that the net cash received oblique disbursed is we have found out is this is amount, so this column is for this and excess or deficit of the cash, if you calculate the excess or deficit of the cash, how much it works out as 27,992 because this shortfall 4,700 is a negative balance but we have 32,692 cash available for operations.

So from this balance available for operations we will adjust the extra of payment of 4,700 so we are left with the balance of 27,992 dollars. This is the amount available with us now and finally we go for the financing arrangement. So, now we surplus amount available with us to the tune of 27,992 to in case of financing arrangements, we are not going to borrow anything from the banks. Loans but it was borrowed in the month of January has already been repaid in the month of February so nothing is to be say repaid back to the bank here.

No interest, similarly no payment for the interest, so total effect of Financing if you look at is going to be, if you look at the total effects of Financing it is going to be almost no effect of the financing and now we have to calculate the closing cash balance. So, closing cash balances how much? 5000 this is the minimum cash balance desired, kept as a safety stock is available with us, plus this amount which is available as excess of the cash of surplus of the cash, so this total become so much 32,992, this is our closing cash balance available at the month of March.

So, finally means after balancing everything, after recording for all the say opening balance of the cash, closing balance of the cash, making the payments then going for the collections from the sales, everything when we prepare the cash budget for the 3 months here for the quarter, so in the one month we found that there is a surplus of 5,100 or maybe you can call it as the extra amount available though it was a deficit in the beginning but when we borrowed from the bank so we got left with 100.

5000 is the minimum cash balance desired that became is the opening balance for the month of February after again keeping 5000 as a minimum cash balance, we are still having 100 rupees, 100 dollars available here and after that when we went for the collections and payment for the purchases and even paying the repaying back the loan back to the bank we were left with the total surface of 37,692 till the end of month of February.

Then we move to the month of March started in opening balance of cash this is a same amount we took to the closing balance for the month of February became the opening balance for the month of March and then we kept again 5,000 is the minimum cash balance so we are left with the cash available for operations for the month of March is 32,692 and after that when we went for say adjusting for the amount for collections and payments so we are left with excess of deficit of cash.

Excess of cash was 27,992 and into this, adding this balance we are left with the closing cash balance for the month of March or you can call it as quarterly closing balance of the cash is positive and that is 32,992 dollars, this is the closing cash balance in one way for the month of March but actually this is the quarterly closing balance of the cash after adjusting everything. So end of the cash budget, quarterly budget for this cash is a positive balance which is 32,992 dollars.

So, now we have completed different schedule, we have completed the schedule for the sales, sales collection, purchase, purchase disbursements, operating expenses were say not very complex so we have directly taken from the case to the cash budget. So, these basic schedules and one statement that is a cash budget is ready with us and now we will have to end up the operating budget part. So end of the operating budget part is as I told you in the previous classes is the income statement or the profit and loss account.

So, end of the operating budget is the income statement and end of the financial budget is the beginning is with the cash budget and end is with the balance sheet. So, now we will prepare these two statements, first is the income statement for this company and then the balance sheet. So, finally we will know that what is the state of profit or loss at the end of this quarter and then we will know the financial position of the company. So, now let us prepare the income statement, so while preparing income statement as I told you that this statement, income statement and balance sheet can be prepared in two formats.

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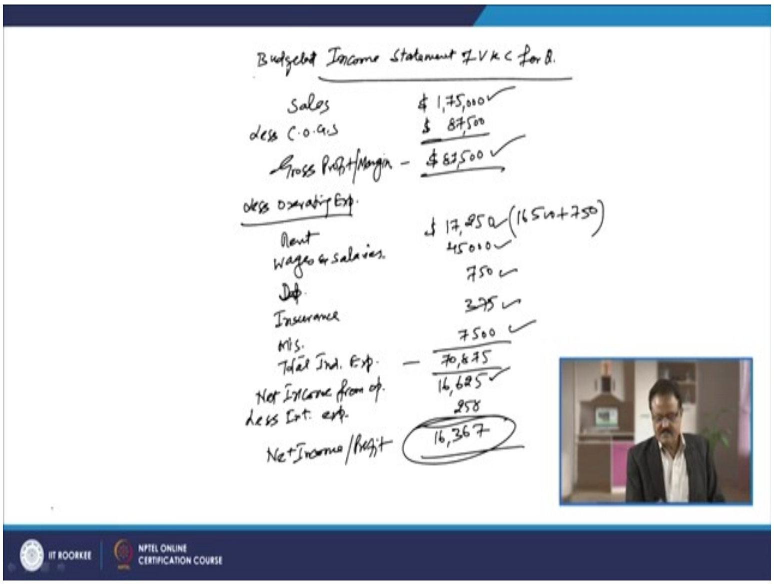

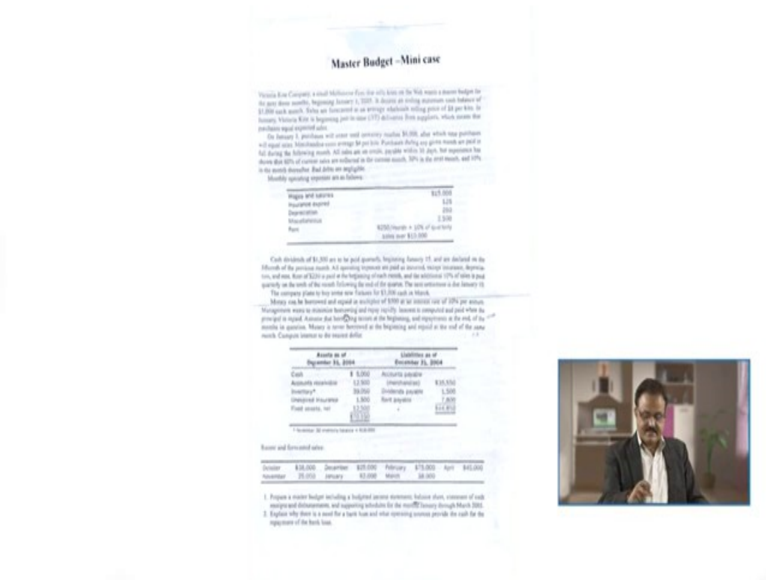

One format is the T format in which we prepared the, in the previous case the profit and loss account and balance sheet, that is T format that is the say format where we have two sides of the column, this is a T format so then you prepare this kind of the format it is called as a T format. In the previous case I have used this format. But in this case I will use the vertical format. In the vertical format we will prepare the income statement same with the balance sheet so you can understand that you can prepare these statements either in the T format which is this or in the vertical format which I am going to prepare now.

So, one think is worth mentioning here that these days now after when we are into the process of convergence of the international financial reporting standards with Indian Standards so now it is decided by The Institute of Chartered Accountants of India and the Indian Ministry of the Corporate Affairs, now that the profit and loss account or the income statement and balance sheets will be prepared in the vertical format. So, that is why now, I am going to show you that how we can prepare the income statements in the vertical format.

Whether it is a quarterly statement or annual statement you can simply convert that quarterly statement into the annual statement when you consolidate the information for all the four quarters into the annual information right. So, let us prepare now the income statement in the vertical format and in this case we will prepare that. So you can write here that Victoria kite company, so it means we will be preparing this income statement in the format which is called as the vertical format, so you can call it as income statement.

Income statement of VKC Victoria Kite Company for the quarter, for the quarter and their quarter is for the month of from January till March. So, we will start in the say from the top, in the top in this statement we put the, see as in case of the T format we have started with the sales, by sales, putting the sales on the credit side of the statement. Again in this statement also we will start with the sales, so will put on the say top is the sales. So we do not use any two or by here, simple we write the sales figure and the total quarterly sales, we have to now find out, so if you calculate the quarterly sales which are given to us, we have already I think found out here, so quarterly sales are how much, this will come up as, total sales are something like 175,000 yes 175000 dollars, these are the quarterly sales.

Less now, simple subtraction so it is a COGS, you will subtract it, so simple subtraction is cost of goods sold first of all, so sales minus cost of goods sold, so what is the cost of goods sold is the merchandise cost and which is half so that amount is how much, this amount is say 87,500, right, 87,500, so this we have subtracted here, so you are left with the balance and that balance is how much that is called as gross margin or the gross profit, we will call it as gross profit so certainly this amount is going to be how much that is a balance 87,500 right.

This is the gross balance or the gross profit or you call it as the gross profit or gross margin, this amount is 87,500 so we are preparing in the vertical format. Now, let us operating expenses, operating expenses, operating expenses, what are operating expenses now, will be calculating now the operating expenses, so we are given the operating expenses in the different statements only we have to sum it up and we have to take the total operating expenses for 3 months, maybe for the quarter as a whole. So, what is the, first item is rent. What is rent, rent I am taking here as now dollars 700, sorry, 17,250, this is rent amount.

So, now you will be wondering how I have taken the rent as 17,250, see now we are preparing this income statement, for the quarter of January to March and the condition in case of the rent is that normal rent for the say per month that is 250 dollars, so 3 months for one quarter it becomes as 750 dollars, plus 10 percent of the sales above the 10,000. So what are the total quarterly sales if you are going to look at now the case? Total quarterly sales for the month of January, February, and this March are going to be there 17,500, right. 17,500, these are the sales given to us, so 175,000 minus 10,000 works out as 16,500 plus 750, so this will come out as, I am saying here that is 10 percent above 10,000 of sales this works out as 16,500 plus 750 is the normal.

So this will come out as the 17,250 is the rent, then we take the next is the wages and salaries, wages and salaries, for this quarter are how much, 45,000 because per month it is 15,000 so simply it is 45,000. Then we talk with the depreciation, so how much is the depreciation. Depreciation is going to be 250 so for three that is 750 dollars, then we are going to talk about is the insurance, how much is insurance that is given to us. Quarterly insurance amount will work out as how much. This will work out as how much was monthly, so you take the insurance amount that amount is given in the case itself, that insurance amount is, insurance expired is 125, so we will have to take this depreciation is 250, so this depreciation and insurance we have not taken in the cash budget because depreciation is a non-cash expense and the insurance, the condition given here is that that has to be all operating expenses are paid as incurred except insurance, depreciation and rent.

Rent of 250 dollar is paid at the beginning of each month and the additional 10 percent of sales is paid quarterly on the 10th of the month following the end the quarter and the next payment is due in the month of January, so we have taken in the cash budget and now the other expenses we have to take here, which I am taking. So we have to adjust for all the expenses, we have taken rent, we have taken wages and salaries, we have taken depreciation, we have taken insurance and this amount works out as how much, 375 is the insurance amount, miscellaneous. Miscellaneous is how much, 7500, this is the total amount. So, if you calculate these expenses they will work out how much.

They will work out as somewhere like 45,000, then 17,250, 750 and 375 this amount will work out as 70,875, right. Now, you can call it as a net income from operations, net income, you will calculate now as net income from operations is how much, that income will be calculated as net income from the operations is 16,000. Now, how much it is, this amount is, we have the gross margin of the 87,500, this is the total you call it as the, total of these all expenses you can call the total indirect expenses, total indirect expenses they come up as 70,875.

So net income this minus this, net income from the operations work out and how much 16,625, right, 16,625 and now one more expense is left here, which we have to subtract is that expense is if you recall that expense is for the interest expense, financial expense. So from this net income from operation, you have to subtract the financial expense, less interest expense, if you take the interest expense, how much is interest expense here 258 dollars which will come from where cash budget because we borrowed, so we return that 15,500 dollars back with the interest of 258, so it means this is the interest we have to subtract.

So, finally you are left with some about which is called as net income, net income/profit right, net income/profit for this quarter is how much, this will work out as, this will be 16,625 minus 258. So this will work out as 16,367, this is the quarterly income or the profit available for this company that is the profit at the end of the month of March. This is the result, this is the report, this is the income for the period of 3 months or for this quarter.

So, finally we have calculated that from the total sales of 175,000 dollars, after subtracting all the cost that is a cost of goods sold plus other operating expenses including depreciation and the insurance which are to be only taken in the income statement, not in the cash flow because depreciation is a non-cash expense, it does not go in the cash budget, insurance was asked to be directly taken to the income statement so we have taken this total, so these figures are for 3 months, all these figures are for 3 months for the quarter, these are not for months. In the cash budget we have taken the monthly figures, these are for the three months all figures.

So, we found out that the total indirect expense was worked out as 70,875 net income from the operations is that is from the gross margin, sales minus cost of goods sold is a gross margin and gross margin minus all indirect expenses or operating expenses is the net income from operations which is 16,625 and from this now if you subtract the other expense that is the financial expense, you call it as the interest expense, interest on the borrowings from the bank, that was calculated as 258 which was given in the cash budget, so finally we are left with the net income, net income or profit for this quarter that is for the quarter of January to march is 16,367.

This is the result of total operations you can say quarterly operations and this is the net result of the operating budget which we started with the sales budget, sales collection budget, purchased budget, purchase disbursement plus other expenses, so sum total, net result of that operating budget is the budgeted income statement and this budgeted income statement is, you can write the word budgeted, we should add here the word budgeted, this is the budget income statement for Victoria Kite Company for the quarter and the net result of this is that we have a surplus or an income or a profit of 16,367.

Now, in this case we are left with one or more statement, last statement which is the end of the financial budget. That is a balance sheet and that balance sheet, that last statement I will prepare in the next class. Thank you very much.