BUDGETING CONTROL

SESSION 3

Advantages of Budgetary Control:

Budgetary control is helpful in setting targets for the whole concern and achievement of the targets. It also makes the various operations of the enterprises economical.

Following are some of the advantages of budgetary control:

1. Maximization of Profits:

Budgetary control aims at increasing the over-all profits of the organization. This is achieved through planning, coordination and control of various activities in a programmed manner.

2. Effective Coordination:

Performance and working of various activities is effectively coordinated through budgetary control. Budgets of the various functions are interlinked and dependent. Effective implementation of budgets depends on cooperation of concerned personnel of various departments. Emphasis on co-ordination and cooperation helps in achieving the predetermined targets and goals.

3. Evaluation of Executive Performance:

Goals are set for each department. Actual performance is compared with standards and deviations are reported to top management for action against unfavorable deviations. Thus, the performance of the department heads and other executives is constantly monitored.

4. Clear-Cut Goals and Targets:

Through the process of budgeting the goals of different departments are set in advance in consultation with those in charge of them. This makes the vision of the organization clear and employee motivation and morale boosted by achievement of clearly set objectives.

5. Economy in Operations:

Expenses are properly planned and financial resources are put to optimum use. The benefits are extended to the industry and then to national economy. Budgetary control is helpful in conservation, effective utilization and elimination of wastage in scarce resources.

6. Revelation of Ineffectiveness:

Comparison of actual performance with budgeted performance reveals week spots so that attention is focused on them to improve the performance.

7. Correction of Performance Continuously:

The deviations of actual performance compared with budgets are frequently reported and corrections are made to rectify the unfavorable deviations immediately. In the absence of budgetary control this may be done at the end of the accounting year by which time corrections may not be fruitful or practicable.

8. Introduction of Incentive Schemes of Remuneration:

Incentive schemes can be easily introduced as the predetermined targets act as base to compare actual performance and determine efficiency. Higher and lower efficiency are suitably rewarded or discouraged respectively.

9. Shutting Down of Unprofitable Products and Activities:

Budgetary control reveals inefficiencies in products, processes and departments. This is helpful in closing down of loss making divisions to improve the overall profitability.

Limitations of Budgetary Control

Budgetary control is an effective tool for management control. However it has certain limitations while operating it as a technique.

1. Prediction of Uncertain Future:

Budgeting is a process of forecasting and estimation. Forecasting may not be accurate. Therefore budgets based on inaccurate forecasts and estimates may not be accurate and effective.

2. Changes of Conditions:

Budgets are prepared on the basis of certain prevailing conditions. If the conditions change budgets are also to be revised. Constant changes in budgets may frustrate the employees and the charm in budgeting and implementation may be lost.

3. Complacence:

General tendency of employees is to achieve the targets as budgeting fixes the targets. Some of the employees who are highly skillful may also be satisfied in performing up to the goals set without showing full potential, which will be a loss to the enterprise as well as the employee in terms of productivity.

4. Difficulty in Coordination:

Effective implementation of budgetary control depends upon proper coordination among various departments as the performance of a department depends on the work of other departments and vice versa. It requires budgetary officer to oversee the integration of various activities to successfully implement the budgets. Ineffective coordination leads to inefficient performance.

5. Conflict among Different Departments:

Budgetary control sets targets for different departments individually. This will make the departmental heads to be selfish to get maximum funds and think in terms of achieving their own set targets, thereby raising conflict among different departments. Inter-departmental rivalries may endanger the performance of the whole organization.

Natarajan Ltd. has four sales territories A, B, C, D. Each salesman is expected to sell the following number of units during the First Quarter of 2003. Assume the Average Selling Price to be Rs. 10:

	Territory			
Month	*A Units*	*B Units*	*C Units*	*D Units*
April	500	750	1,250	1,750
May	1,000	900	1,400	2,000
June	1,250	1,000	1,500	2,250

Solution:

Sales Budget, First Quarter 2003

Territory	*April*			*May*			*June*			*Quter*	
	Qty. unit	*Price Rs.*	*Value Rs.*	*Qty. unit*	*Price Rs.*	*Value Rs.*	*Qty. unit*	*Price Rs.*	*Value Rs.*	*Qty. unit*	*Value Rs.*
A	500	10	5,000	1,000	10	10,000	1,250	10	12,500	2,750	27,500
B	750	10	7,500	900	10	9,000	1,000	10	10,000	2,650	26,500
C	1,250	10	12,500	1,400	10	14,000	1,500	10	15,000	4,150	41,500
D	1,750	10	17,500	2,000	10	20,000	2,250	10	22,500	6,000	60,000
Total	4,250		42,500	5,300		53,000	6,000		60,000	15,550	1,55,500

From the following particular, you are required to prepare production budget of

Mrs. V. G. P. Ltd. a manufacturing organization that has three products X, Y and Z

Product	*Estimated Stock at the beginning of the budget period*	*Estimated Stock at the end of the budget Period*	*Estimated Sales as Per sales budget*
X	5,000 units	6,400 units	21,600 units
Y	4,000 units	3,850 units	19,200 units
Z	6,000 units	7,800 units	23,100 units

Solution:

Particulars	*X (Units)*	*Y (Units)*	*Z (Units)*
Expected Sales during the period	21,600	19,200	23,100
Add : Closing stock at the end of budget period	6,400	3,850	7,800
	28,000	23,050	30,900
Less : Opening stock at the beginning of the budget period	5,000	4,000	6,000
Budgeted Production	23,000	19,050	24,900

A company is expecting to have Rs. 25,000 cash in hand on Ist April 2003 and it requires you to prepare an estimate of cash position in respect of three months from April to June 2003, from the information given below :

	Sales *Rs.*	*Purchase* *Rs.*	*Wages* *Rs.*	*Expenses* *Rs.*
February	70,000	40,000	8,000	6,000
March	80,000	50,000	8,000	7,000
April	92,000	52,000	9,000	7,000
May	1,00,000	60,000	10,000	8,000
June	1,20,000	55,000	12,000	9,000

Additional Information :

(a) Period of credit allowed by suppliers — two months.
(b) 25 % of sale is for cash and the period of credit allowed to customer for credit sale one month.
(c) Delay in payment of wages and expenses one month.
(d) Income Tax Rs. 25,000 is to be paid in June 2003.

Solution:

Cash Budget

Particulars	*April* *Rs.*	*May* *Rs.*	*June* *Rs.*	*Total* *Rs.*
Opening balance of cash	25,000	53,000	81,000	1,59,000
Cash Respects :				
Cash Sales	23,000	25,000	30,000	78,000
Debtors	60,000	69,000	75,000	2,04,000
Total Cash Receipts – (1)	1,08,000	1,47,000	1,86,000	4,41,000
Cash Payments :				
Creditors	40,000	50,000	52,000	1,42,000
Wages	8,000	9,000	10,000	27,000
Expenses	7,000	7,000	8,000	22,000
Income tax	–	–	25,000	25,000
Total Payment – (2)	55,000	66,000	95,000	2,16,000
Closing Balance of Cash (1-2)	53,000	81,000	91,000	2,25,000

The expenses budgeted for production of 10,000 units in a factory are furnished below :

	Per unit *Rs.*
Materials	70
Labour	25
Variable factory overheads	20
Fixed factory overhead (Rs. 1,00,000)	10
Variable expenses (Direct)	5
Selling expenses (10 % Fixed)	13
Distribution expenses (20 % Fixed)	7
Administrative expenses (Rs. 50,000)	5
Total cost of sale per unit	155

You are required to prepare a budget for the production of 8,000 units.

Solution:

Flexible Budget

Particulars	*Output 10,000 units*		*Output 8,000 units*	
	Per unit	*Amount*	*Per unit*	*Amount*
Variable Expenses :				
Material cost	70	7,00,000	70	5,60,000
Labour cost	25	2,50,000	25	2,00,000
Direct expenses (variable)	5	50,000	5	40,000
Prime cost	100	10,00,000	100	8,00,000
Add : Factory overheads :				
Variable overheads	20	2,00,000	20	1,60,000
Fixed overheads	10	1,00,000	12.50	1,00,000
Works cost	130	13,00,000	132.50	10,60,000
Add : Administrative expenses				
Fixed (Assumed)	5	50,000	6.25	50,000
Cost of production	135	13,50,000	138.75	11,10,000
Add : Selling Expenses				
Fixed – 10 % of Rs. 13	1.30	13,000	1.63	13,000
Variable – 90 % of Rs. 13	11.70	1,17,000	11.70	93,600
Add : Distribution Expenses:				
Fixed – 20 % of Rs.7	1.40	14,000	1.75	14,000
Variable – 80 % of Rs.7	5.60	56,000	5.60	44,800
Total Cost of Sales	155	15,50,000	159.43	12,75,400