UNIT-1
Accounting for managers

Introduction:

- The accounting for managers is also called management accounting.
- The management accounting has been developed to cope with the limitation of financial accounting and cost accounting.

Meaning:

- Management accounting is the presentation of accounting information is such a way as it assists the management in the creation of policy and the day-today operation of an undertaking and to evaluate the impact of its decisions and actions.
- The data required for this purpose collected with help of financial accounting and cost accounting by the management.

Definition:

Management accounting concerned with accounting information that is useful to management.

Nature:

i) Technique of selection nature:

Management accounting is a technique selective nature it takes into consideration only that data from the income statement and financial position from the income statement and financial position statement which is relevant and useful to the management. That information is communicated to management to take decisions on various aspects of business.

ii) Provides data and not the decisions:

The management accountant does not take any decision but provides data which is helpful to the management in decision-making.

iii) Concerned with future:

The management accounting deals with the forecast and the future. It helps the management in planning the future.

iv) Analysis of different variables:

Management accounting helps in analysis the reasons like why theprofit or loss is more or less as compared to the past period. It tries to analyses the effect of different variables on the profits and profitability of the business.

v) No set formals for information:

The management accounting will not provide information in a prescribed preformed like that of financial accounting.

vi) <u>It modifies analyses and interprets data:</u>

The management accounting is more concerned with the analysis and interpretation of past events. This data is used to take new decisions for the future by the management.

<u>Scope:</u>

The following are the field of activities included in the scope

i. <u>Financial accounting:</u>

Financial accounting provides historical data but it is useful for financial forecasting and future planning.

ii. <u>Cost accounting:</u>

It provides various techniques of costing live marginal costing, standard costing opportunity cost analysis etc which play a useful role in the operation and control of the business under takings.

iii. <u>Budgeting and forecasting:</u>

Forecasting on the various aspects of the business is necessary for budgeting business by comparing actual figures with the budgeted figures to find out the deviations analysis the deviations in order to find out exact responsibility and takes remedial action.

iv. <u>Cost control procedures:</u>

These procedures are integral part of the management accounting process and include inventory control, cost control, budgetary control, labour control, variance analysis etc.

v. <u>Reporting:</u>

The management accountant is required to submit reports to the management on the various aspects of the business. For this per pose he uses statistical tools for presentation of information as graphs, charts, pictorial, presentation, Indies numbers and offer devices in order to make it more impressive and intelligent.

vi. Methods and procedures:

It includes in this study all these methods and procedures which help the business firm to use its resources in the mass efficient and economical manner. It under takes special cost studies, estimations and reports in cost volume profit relationship under changing circumstances.

vii. Tax accounting:

It is an integral part of management accounting and includes preparation of income statement, determination of taxable income.

viii. Internal financial control:

Management accounting includes the internal control methods like internal audit, efficient office management etc.

ix. Interpretation:

Management accounting is closely related to the interpretation of financial data to the management and accusing them on decision-making.

x. Office services:

The management accountant may be required to maintain and control office services in some organizations this function include data processing , reporting on best use of mechanical and electronic devices , communication etc.

xi. Evaluating the performance of the management:

Management accounting precedes methods and techniques for evaluating the performance of the management.It evaluates the performance of the management to archive the adjectives of management.

Management process and accounting

- Management accounting is the process of identification, measurement, accumulation, analysis, preparation, interpretation and communication of financial information used by management.
- This is used by management to plan evaluate and control within an organization and to assure appropriate use of and accountability for its resources.
- Management accounting also comprises the preparation of financial reports for management groups such as shareholders,creditors, regular agencies tax authorities.

The following are the activities will be done for this purpose.

i) Identification:

It includes the regression and evolution of business transactions and other economic events for appropriate accounting action.

ii) Measurements:

It includes estimation of business transaction or other economic events that have occurred or may occur.

iii) Accumulation:

The disciplined and consistent approach to be used to record and classify the gathered appropriate business transactions and other economic events.

iv) Analysis:

It includes the determination of resources for and relationships of the reported activity with other economic events and circumstances.

v) Preparation and interpretation:

The meaningful coordination of accounting or planning data is necessary to identify the needed information and presented in a logical format and interpreted to the management.

vi) Communication:

The reports are communicated to the management and other.

Cost accounting vs Accounting for management

The main dissection between cost accounting and management accounting are as follows.

a) **Deals with:**

Cost counting: It deals with the ascertainment, allocation, apportionment and accounting aspect of casts.

Management accounting: It deals with the effect and impact of cost on the business.

b) **Base:**

Cost accounting: If provides a base for management accounting.

Management accounting: It derived from both cost accounting and financial accounting.

c) **Role:**

Cost accounting: It is helpful in collecting casting data for the management.

Managements accounting: The management accountant has clear idea of types of costs and items requiring analysis and states the specific problems of business.

d) **Status:**

Cost accounting: Thestate of cost accountant comes after management accountant.

Management accounting: The management accountant is a senior in position to cost accountant.

e) **Out looks:**

Cost accounting: The cost accountant has to refer to economic and statistical data for analyzing cost effects.

Management accounting: The management accountant reports the effect of cost on the business along with cost analysis.

f) **Tools & techniques:**

Cost accounting: It has standard costing, variable costing, breakeven analysis etc as the basic tools and technique.

Managementaccounting:Along with tools and technique of cost accounting, the management accountant has funds and cash flow statements ratio analysis as his accounting tools and techniques.

g) **Scope:**

Cost accounting: It does not include financial accounting tax planning and tax accounting.

Management accounting: It includes financial accounting, cost accounting, tax planning and tax accounting.

h) Period of planning:

Cost accounting: It is concerned with the short form planning.

Management accounting: It is concerned with sort range and long range planning and uses techniques like sensitivity, analysis, probability structure etc.

i) Assistance:

Cost accounting: It merely assists the management in its functions.

Management accounting: It assists and evaluates the management performance.

Role Accountant in Modern organization

i) Designing works:

It includes the designing of the accounting system, basis for identification and classification of financial transaction and events, forms, methods and procedures etc.

ii) Recording works:

The financial transactions are identified, classified and recorded in appropriate books of accounts according to principles, policies, methods and procedures. This is "book-keeping".

iii) Summarization works:

The recorded transactions are summarized into significant form according to generally accepted accounting principles. The work includes the preparation of profit & loss account, balance sheet and funds flow and cash flow statements. The phase is also called as "preparation of final account'.

iv) Analysis and interpretation work:

The summarized statements are analyzed with the help of stastical tools. Then these statements are interpreted according to accounting standards and the laws. This is the analysis of financial statements.

v) Reporting work:

The summarized statements along with analysis and interpretation are communicated to the interested parties. In addition, the accounting department has to prepare and send regular or intern reports so as to assist the management in decision making. "This is Reporting"

vi) Preparation of budget:

The management must be able to reasonably estimate the future requirements and opportunities. The accounting department has to prepare budgets, like cash budget, capital budget, purchases budget, sales budget etc... "This is Budgeting"

vii) Taxation work:

The accountant has to prepare various statements and returns pertaining to income-tax, sales tax, excise or customs, duties etc.

viii) Auditing:

It includes a critical review and verification of the books of accounts, statements and reports with a view to verifying their accuracy. "This is Auditing'

Financial accounting vs Cost accounting

The main difference between Financial accounting and Cost accounting are as follows.

a) Purpose:

Financial accounting: It tells about the profit and loss and financial position of the business to owners and other outside parties.

Cost accounting: It provides cost information to the management for proper planning, operation, control and design making.

b) Form of accounts:

Financial accounting: These accounts are kept n such a way as to meet the requirements of the companies act and income tax act.

Cost accounting: These accounts are kept voluntarily to meet the requirements of the management. But now companies act has made it obligatory to keep cost records in some manufacturing industries.

c) Recording:

Financial accounting: It classifies, records and analysis the transactions in a subjective manner i.e. according to the nature of expenses.

Cost accounting: It records the expenditure in an objective manner i.e. according to the purposes for which the costs are incurred.

d) Control:

Financial accounting: It gives emphasis on the recording aspect without attaching any importance to control.

Cost accounting: It provides a detailed system of control for materials, labour and overhead costs with the help of standard costing and budgetary control.

e) **Periodicity of reporting:**

Financial accounting: It reports operating results and financial position usually at the end of the year.

Cost accounting: It gives information through cost reports to management as and when desired.

f) **Analysis of profit:**

Financial accounting: Financial accounts are the accounts of the whole business. They are independent in nature and disclose the net profit or loss of the business as a whole.

Cost accounting: Cost accounting only parts of the financial accounts and disclose profit or loss of cash product, job or service.

g) **Reporting of costs:**

Financial accounting: The costs are reported in aggregate in financial accounts.

Cost accounting: The costs are broken down on a unit basis in cost accounts.

h) **Nature of transactions:**

Financial accounting: Financial accounts are concerned with external transactions i.e. transactions between thee business concern on one side and third parties on the other. These transactions form the basis for the payment or receipt of cash.

Cost accounting: It is concerned with the internal transactions which do not form the basis for the payment or receipt of cash.

i) **Information:**

Financial accounting: Only the monetary transactions are recorded in final accounts.

Cost accounting: It deals with the monetary and non-monetary information.

j) **Fixation of selling price:**

Financial accounting: Financial accounts are not maintained with the object of fixing selling prices.

Cost accounting: It provides sufficient data for fixation of selling price.

UNIT-2
Financial Accounting System

The main objective of an accounting system is to reveal the results and financial position of the business. With this objective in view every trader will prepare accounts at the end of each year.

Such accounts which are prepared to know the profit or loss and the financial position, it is known as Final accounts.

The final accounts of business involves preparation of two statements known as

a) Income statement
b) Position statement

(a) Income statement consists of

i. Trading account
ii. Profit & loss account

(b) Position statement also known as Balance sheet discloses the financial position of the business.

Generally accepted accounting Principles

Generally accounting principles may be classified into two categories.

i. Principles to be observed at the time of recording transactions (Recording stage)
ii. Principles to be observed at the time of preparing the final accounts (Reporting stage)

i) The Principles at the Recording stage

a) Business entity concept (principle)
b) Money measurement principle
c) Objective widence principle

d) Historical record principle
e) Cost principle
f) Dual aspect principle

(a) Business entity concept (principle):

This principle implies that the business in distinct from the persons who own it. If the owner takes any cash (or) goods from the business the drawings account is debited and cash (or) goods account is credited. Otherwise, the personal and business transactions will get mixed up and the accounting statements become confused.

(b) Money measurement principle:

While recording the business transactions, we do not record them in terms of kilograms, quintals, meters, liters etc. we record them in a common denomination. So as to see that their total becomes homogeneous and meaningful. Money does this function.

(c) Objective widence principle:

All accounting transactions should be evidenced and supported by documents such as invoices, receipts, cash memo etc.

(d) Historical record principle:

The account shows only those transactions which have actually taken place in the past.

(e) Cost principle:

Usually all the transactions will be recorded at cost in the books. However, at the end of every year the account shows the reduced value of the asset, after providing for depreciation.

(f) Dual aspect principle:

This principle throws to get on the point that cash transaction has two fold effects - the receiving of the benefit and giving of the benefit. The receiving aspect is termed as debit, where as the giving aspect as credit.

ii) The Principles at the Reporting stage

a) Going concern principle
b) Accounting period principle
c) Matching principle
d) Conservation principle
e) Consistency principle
f) Full disclosure principle
g) Materiality principle

(a) <u>Going concern principle:</u>

It is assumed that the business will continue for a long time with this assumption fixed assets are recorded in the books at the original cost.

(b) <u>Accounting period principle:</u>

To facilitate the business concern to arrive at an opinion about the profit or loss every firm will have an accounting period.

(c) <u>Matching cost principle:</u>

This principle deals with the matching of costs, the first being the revenue recognition. In determining net income from business operation all costs which are applicable to revenue of the period should be charged against the revenues.

(d) <u>Conservation principle:</u>

This principle warns the trader not to take unrealized income into account. That is why the practice of valuing stocks at cost (or) market price whichever is lower is in practice.

(e) <u>Consistency principle:</u>

The methods or principles followed in the preparation of various accounts should be followed in the years to come. It means that there should be consistency in the methods or principles followed.

(f) <u>Full disclosure principle:</u>

This principle deals with the connection that all information which of material importance should be disabled in the accounting statements.

(g) <u>Materiality principle:</u>

Under this principle the trader records important facts about the commercial activities in the form of financial statements.

Analysis and Interpretation of financial statements

- Analysis of financial statement refers to the art of applying various tools to know the behavior of the accounting information.
- According to "Kennady and muller analysis and interpretation of financial statements are an attempt to determine the significance and meaning of the financial statement data".
- Analysis: It implies the classification of facts or data in a logical order. It involves splitting the complex data into various simple elements.
- Interpretation: It implies explaining the meaning and significanceof the facts or data so classified.

Tools (or) Techniques (or) Methods of Financial Analysis

i) Comparative financial statements:

The comparative financial statements as the name itself suggests enable comparison of financial information for two or more years placed side by side. From this it is possible to appraise the performance, position and efficiency of business.

ii) Common-size financial statement analysis:

The common-size financial statements are most valuable in making comparison between the firms in e same industry. The two common-size financial statements usually prepared are,

a. common-size income statement
b. common-size balance statement

iii) Trend analysis or Trend ratios:

Trend ratios can be defined as the index members of the movements of the various financial items on the financial statement for a number of periods.

$$\text{Formula} = \frac{\text{Absolute value of item in the statement under study}}{\text{Absolute value of the same item in basic}} \times 100$$

iv) Ratio analysis:

Ratio analysis is the process of determining and interpreting numerical relationship based on financial statements. It is the technique of interpretation of financial statements with the help of accounting ratio desired from the balance sheet and profit and loss account.

v) Funds flow analysis:

The funds flow analysis is a technical device designed to analyze the changes in the financial condition of a business enterprise between two dates. It is also called a statement of sources and application of funds as it describes the sources and application of working capital and highlights the basic changes in the resources and financial structure of a concern.

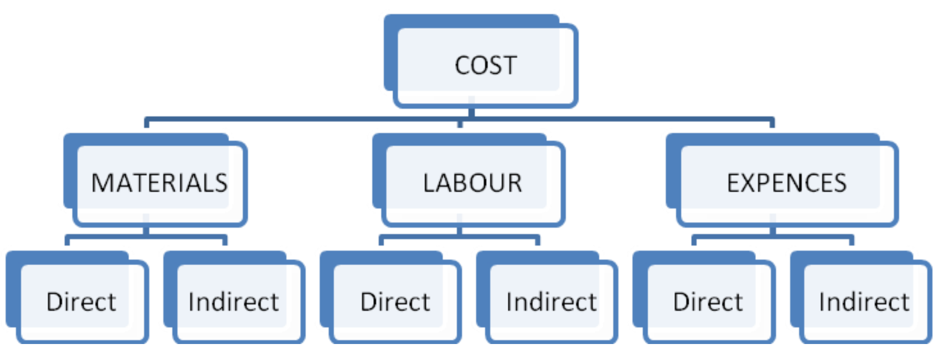
vi) Cash flow analysis:

It shows the changes in the cash position between two dates of balance sheet. The change in cash position is known by considering the inflow and outflow of cash.

UNIT-3
Elements of cash

According to "ICMA" cost means, "the amount of expenditure incurred on a specified thing or activity".

The elements of cost are the essential parts of the cost. There are broadly three elements of cost as explained below.



Material:

The substance from which the product is made is called material. It can be direct as well as indirect.

Direct material: It refers to those materials which become an integral part of the financial product and can be easily traceable to specific physical units.

Direct material includes the following.

i) All material specifically purchased for a particular job or process
ii) Components purchased or produced
iii) Primary parking materials (Ex:- carton, cardboard, boxes etc)
iv) Material passing from one process to another

Indirect material: All material which is used for main activities to the business and which cannot conveniently be assigned to specific physical units is known as Indirect material.

Ex:- oil, grease, consumable stores, stationary and material etc.

Labour:

In order to convert materials into finished products, human effort is required such human effort is known as labour. Labour can be direct as well as indirect.

Direct labour: it is defined as the wages paid to workers who are engaged in the production process and whose time can be conveniently and economically traceable to specific physical units.

Indirect labour:Labour employed for the purpose of carrying out tasks incidental to goods produced to services provided is called Indirectlabour.

Ex:- wages of store-keepers, foremen, supervisors etc.

Expenses: Expenses may be direct or indirect.

Direct expense: these are expenses which can be directly, conveniently and wholly identified with a job, process or operation. Direct expenses are also known as chargeable expenses or productive expenses.

Ex:- cost of layout, design, drawings etc.

Indirect expenses: Expenses which cannot be changed to production directly and which are neither indirect materials nor indirect wages are known as Indirect expenses.

Ex:- rent, rates and taxes, depreciation, repairs and maintenance etc.

Absorption costing vs Marginal costing

Absorption costing	Marginal costing
1. All costs both fixed and variable costs are included for ascertaining the cost.	1. Only variable costs are included. Fixed costs are recovered from contribution.
2. Different unit costs are obtained at different levels of output because of fixed expenses remaining same.	2. Marginal cost per unit will remain same at different levels of output because variable expenses vary in the same proportion in which output varies.
3. Difference between sales and total cost is profit.	3. Difference between sales and variable cost is contribution and fixed cost is profit or loss.
4. Stocks of work in progress and finished goods are valued at full or total cost.	4. Stocks of work in progress and finished goods are valued at marginal cost.
5. The apportionment of fixed expenses on an arbitrary basis gives rise to over or under absorption of overheads.	5. Only variable costs are charged to products, marginal cost technique does not lead to over or under absorption of fixed overhead.
6. Costs are classified according to functional basis such as production cost, administration cost, selling and distribution cost.	6. Costs are classified according to variability.

Cost-Volume-Profit Analysis (Or) Break Even Analysis

- Breakeven means to complete a piece of business without making any loss.

- Break even analysis involves the study of costs and revenues of a business firm in relation to its sales volume.Specially it is the determination of that volume at which the costs and revenues will be equal.
- The term Break even analysis is interpreted in the narrower as well as broader sense.
- Used in its narrower sense, it is concerned with finding out the breakeven point i.e. level of activity where the total cot equals total selling price.
- In broader sense, it means that system of analysis which determines the probable profit at any level of production.
- The Breakeven analysis establishes the relationship of costs, volume and profit. So this analysis is also known as "Cost-Volume-Profit" analysis.

  Objectives of Cost-Volume-Profit analysis:

  i. This analysis helps to forecast profit fairly accurately as it is essential to know the relationship between profits and costs on one hand and volume on the other.
  ii. To facilitate in the preparation of flexible budgets.
  iii. To evaluate the performance of the business. For evaluating the profit earned and cost increased, it is necessary to know the impact of cost on the determining the pricing policies.
  iv. To enable management in determining the pricing policies.
  v. To enable the charging of overheads to cost of production at different levels of production.

- The study of cost-volume-profit can be made by,
  a) Mathematical relationship between cost, volume and profit
  b) By preparing break even charts
- In order to understand mathematical relationship between cost, volume and profit, it is desirable to understand the following four concepts.
  i) Contribution
  ii) Contribution/sales (or) profit-volume ratio
  iii) Breakeven point
  iv) Margin of safety

i) Contribution:

Contribution is the difference between the sales and marginal cost of sales (variable cost of sales) and it contributes towards fixed expenses and profit.

Contribution = Selling price – Variable cost (marginal cost)
(Or) Contribution = Fixed expenses + Profit / - Loss

ii) Contribution/sales (or) profit-volume ratio:

P/V ratio	=	Contribution / Sales
(Or)	=	(Fixed expenses + Profit) / Sales
(Or)	=	(Sales - Variable cost) / Sales
(Or)	=	change in profits or contributions / change in sales

iii) Break-even point:

- The main objective of the break-even analysis is not simply spot the B.E.P, but to develop an understanding of the relationships of cost, price and volume within a company's practical range of operations.
- As coming to the determination of breakeven point, it can be determined either in terms of physical units or in terms of money i.e. sales value in rupees.

a) Breakeven point in terms of physical units:-

- This method is convenient for single-product firms. The break-even volume is the number of units of the product which must be sold to earn enough revenue just to cover all expenses – both fixed and variable costs.
- The selling price of a unit covers not only its variable cost but also leaves a margin i.e. contribution margin to contribute towards the fixed costs.
- The break-even point is reached when sufficient number of units has been sold so that the total contribution margin of the units sold is equal to the fixed costs.
- The formula for calculating the break-even point is,

B.E.P = Fixed costs / Contribution margin per unit

Contribution margin = Sales – Variable cost

(or) = Fixed cost + profit / - loss

b) Breakeven point in terms of sales value:-

- This method is convenient for multi-product firms, because they are not in a position to measure the break-even point in terms of any common unit of product. So they find it convenient to determine their break-even point in terms of total rupee sales.

- B.E.P = Fixed costs / Contribution margin ratio

  Contribution margin ratio (or) Profit-volume ratio = $\frac{\text{Sales - Variable cost}}{\text{Sales}}$

iv) Margin of safety:

- Margin of safety is the difference between the actual sales and the sales at break-even point.
- Margin of safety is that sales which give us profit after meeting fixed costs.

Margin of safety = Actual sales – Break even sales

(or)

$\frac{\text{Profit}}{\text{P/V ratio}}$

UNIT-4

- Decision making is a process of choosing among a set of alternative courses of action with a view to attain the firm's objective.
- A manager should take the following steps to make decisions intelligently and skillfully.
  i) He should recognize the problems for which decisions have to make
  ii) He should identify the alternative ways of solving the problems
  iii) He should evaluate the alternatives by analyzing their costs and benefits
  iv) He should adopt the most profitable courses of action based on his evaluation

Decision making situations:

- Decision-making is a future oriented activity, it involves forecasting and planning.
- The following are the various decision situations
  i. Pricing and special order pricing
  ii. Sell or further process decisions
  iii. Make / buy decisions
  iv. Product decisions
  v. Plant shut down decisions

i) Pricing and special order pricing:

- ➢ Ordinarily the firms quote full cost based prices for their products when demand is relatively regular and stable.
- ➢ Other important factors influencing pricing decisions are – market forces, trade customs and management's pricing strategy.
- ➢ Firms are sometimes faced with special pricing situations which are of non recurring nature.

  Ex:- price may have to be fixed for special orders when the firm has an idle capacity and demand for its product is very low
- ➢ The contribution approach is particularly useful in establishing prices for special orders.

ii) Sell or further process decisions:

- A product can be sold by a company when it has been partially processes or if processing it further and then selling it.
- When a product passes through a series of manufacturing operations, it may be a saleable product at a number of different points along the way.
- Thus a company has an option to sell the product at various physical stages of competition.

  Ex:- In petroleum refinery, the refinement of oil can be stopped at several points during the process and can be sold as fuel oil, diesel oil, kerosene or gasoline as market exists for all these intermediate semi-manufactured products.

iii) Make /Buy Decision:

- In assembly type of business firms, different components parts are assembled in order to manufacture the product. Such component parts can be manufactured in the business firm or these can be purchased from external supplies.
- If the business firm has idle capacity and idle workers that can be used to make component parts, it is preferable to make and realize cost savings.
- If there is no idle capacity, the parts can be purchased from the outside.

iv) Product Decision:

- When a factory manufactures more than one product, a problem is faced by management as to which product mix will give the maximum profits. The best product mix is that which yields the maximum contribution.

v) Plant shut down decisions:

- Sometimes it becomes necessary for a firm to temporarily suspend or close the activities of a particular product, department or factory as a whole due to trade recession.

Budget:

It is a financial and /or quantitative statement prepared to a definite period of time of the policy to be pursued during that period for the purpose of attaining a given objective.

Types of Budget:

Budgets can be classified according to various points of view, the following basis of classification are generally followed in practice.

a) Functional classification
b) Classification on the basis of time factor
c) Classification on the basis of flexibility

a) <u>Functional classification:</u>

A master budget is the summary budget for the entire enterprise and embodies the summarized figures for various activities. It is the consolidation of all functional budgets.

UNIT-5
Budgeting

Meaning of Budget:

- A budget is a detailed plan of operations for some specific future period.
- It is an estimate prepared in advance of the period to which it applies.

Budget, Budgeting And Budgetary Control:

A budget is a blue print of a plan expressed in quantitative terms. Budgeting is a technique for formulating budgets. Budgetary control, on the other hand, refers to the principles, procedures and practices of achieving given objectives through budgets.

Rowtand and Willium have differentiated the three terms as: "Budgets are the individual objectives of a department, etc., where as Budgeting may be said to be the act of building budgets. Budgetary control embraces all and in addition includes the science of planning the budgets to affect an overall management tool for the business planning and control.

Characteristics of Budget:

1) It is prepared in advance.
2) It is based on future plan of actions.
3) It is a statement expressed in monetary/ physical units.
4) Budgets are the individual objectives of a department etc.
5) Budgeting may be defined as the act of building budgets.

Budgeting control embraces all and in addition includes the science of planning the budgets themselves and the utilization of such budgets to effect an overall management control for the business planning and control.

Nature and Scope of Budgetary Control:

1. Budgetary control is the process of determining various budgeted figures for the enterprise for the future period.
2. Comparing the budgeted figures with the actual performance for calculating variances.
3. It is a continuous process which helps in planning and coordination.
4. It provides a method of control.
5. Objectives are set by preparing budgets.
6. The actual figures are recorded.
7. The budgeted and actual figures are compared for studying the performance of different cost centers.
8. If actual performance is less than the budgeted norms, a remedial action will take immediately.

Advantages of Budgetary Control:

The budgetary control system helps in fixing the goals for the organization as a whole and concerted efforts are made for its achievements. It enables economics in the enterprises. Some of the advantages of budgetary control are:

1) **Maximization of profit:**

The budgetary control aims at the maximization of profits of the enterprise. To achieve this aim, a proper planning and co-ordination of different functions is undertaken. There is a proper control over various capital ad revenue expenditures. The resources are put to the best possible use.

2) **Co-ordination:**

The working of different departments and sectors is properly coordinated. The budgets of different departments have a bearing on another. The co-ordination of various executives and subordinates is necessary for achieving budgeted targets.

3) **Specific aims:**

The plans, polices and goals are decided by the top management. All efforts are put together to reach the common goal of the organization. Every department is given a target to be achieved. The efforts are directed towards achieving some specific aims. If there is no definite aim then the efforts will be wasted in pursuing different aims.

4) **Tool for measuring performance:**

By providing targets to various departments, budgetary control provides a tool for measuring managerial performance. The budgeted targets are compared to actual results and deviations are determined.

5) **Economy:**

The planning of expenditure will be systematic and there will be economy in spending. The finances will be put to optimum use. The benefits derived for the concern will ultimately extend to industry and then to national economy. The national resources will be used economically and wastage will be eliminated.

6) **Determining weaknesses:**

The deviations in budgeted and actual performance will enable the determination of weak sports. Efforts are concentrated on those aspects where performance is less than the stipulated.

7) **Corrective action:**

The management will be able to take corrective measures whenever there is a discrepancy in performance. The deviations will be regularly reported so that necessary action is taken at the earliest. In the absence of a budgetary control system, the deviations can be determined only at the end of the financial period.

8) **Consciousness:**

It creates budget consciousness among the employees. By fixing targets for the employees, they are made conscious of their responsibility. Everybody knows what he is expected to do and he continues with his work uninterrupted.

9) **Reduces costs:**

In the present day competitive world, budgetary control has a significant role to play. Every businessman tries to reduce the cost of production for increase in sales. He tries to have those combinations of products where profitability is more.

10) **Introduction of Incentive schemes:**

Budgetary control system also enables the introduction of incentive schemes of remuneration. The comparison of budgeted and actual performance will enable the use of such schemes.

Limitation of Budgetary control:

Despite many good points of budgetary control there are some limitations of this system. **Some of the limitations are discussed as follows:**

1) **Uncertain future:**

   The budgets are prepared for the future period. Despite best estimates made for the future, the predictions may not always come true. The future is always uncertain and the situation which is presumed to prevail in future may change.

2) **Budgetary Revisions Required:**

   Budgets are prepared on the assumptions that certain conditions will prevail. Because of future uncertainties, assumed conditions may not prevail necessitating the revision of budgetary targets.

3) **Discourages Efficient persons:**

   Under budgetary control system the targets are given to every person in the organization. The common tendency of people is to achieve the targets only.

4) **Problem of Co-ordination:**

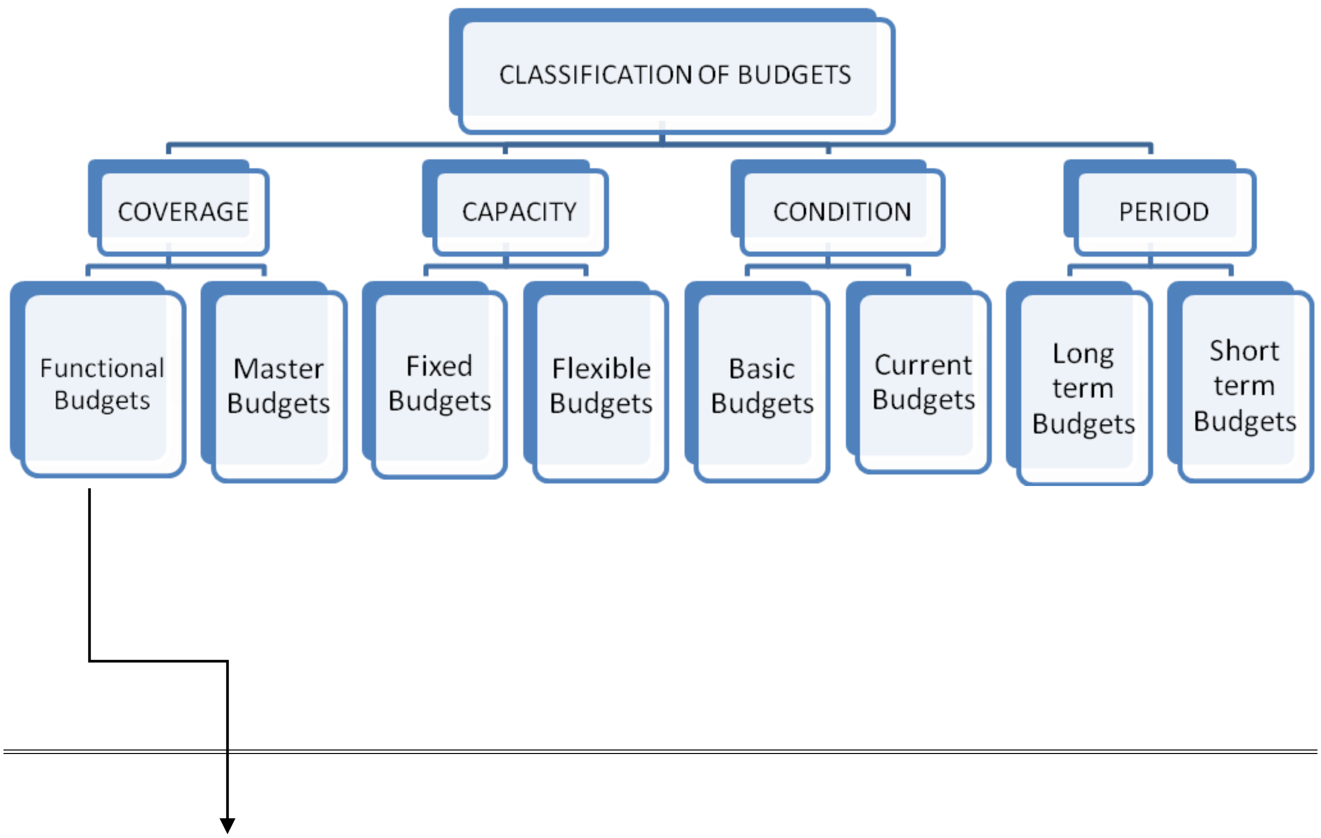
   The success of budgetary control depends upon the co-ordination among different departments. The performance of one department affects the results of other departments. To overcome the problem of co-ordination a budgetary officer is needed.

5) **Conflict among different departments:**

   Budgetary control may lead to conflicts among functional departments. Every departmental head worries for his department goals without thinking of business goals.

6) **Depends upon support of top management:**

   Budgetary control system depends upon the support of top management. The management should be enthusiastic for the success of this system and should give full support for it. If at any time there is a lack of support from top management, then this system will collapse.



1) Sales budget
2) Production budget
3) Material budget
4) Labour& Personnel budget
5) Manufacturing budget
6) Administration cost budget
7) Plant utilization budget
8) Capital expenditure budget

9) Research & development cost budget
10) Cash budget
11) Selling & distribution cost budget

Functional Budgets:

1. **Sales Budget**:

A sales budget is an estimate of expected sales during a budget period. A sales budget is known as a nerve centre or backbone of the enterprise. The degree of accuracy with which sales are estimated will determine the practicability of operating budgets. A sales budget is the starting point on which other budgets are also based.

A sales budget lays down potential sales figures in value as well as in quantity. It lays down a comprehensive plan and program for sales department. The sales manager is made responsible for preparing sales budget. He uses all possible information available from internal and external sources.

2. **Production Budget:**

The Production budget is prepared in relation to the sales budget. Whatever is to be sold should be produced in time so that it is delivered to the customer. It is a forecast of the production for the budget period. Production budget is prepared for the number of units to be produced and also for the cost to be incurred on materials, labour and factory overheads.

3. **Material Budget:**

The material budget is concerned with determining the quantity of raw materials required for production. The program for purchasing raw materials is adjusted according to the production budget.

The materials are purchased as per the requirements of production department. The requirements of consumption of raw materials are also determined. The number of units to be produced multiplied by the rate of consumption will give the figure of materials required. The stocks of materials required in hand at any time are added to the materials required for production. The opening stock of materials is deduced from the figures determined as above. In this way, therequirement of materials in units will be determined. The units of materials required multiplied by the rate per unit of raw material will give us a figure of material cost.

4. **Labour& Personnel Budget:**

The labour required for production may be classified into direct and indirect labour. The labour required for manufacturing the product is known as direct labour. The labour which cannot be specified with production is called indirect labour.

Labour budget is useful for anticipating labour time required for production. The personnel department is also able to make arrangements for requirement of workers etc.

5. **Manufacturing overhead Budget:**

The manufacturing overheads cost is that part of works cost which arises from indirect labour, indirect materials, overheads and other factory expenses. Manufacturing cost is excluded from direct material and direct labour. Manufacturing overheads cost may be classified into fixed cost, variable cost and semi-variable cost.

6. **Capital Expenditure Budget:**

The budget lays down the amount of estimated expenditure to be incurred on fixed assets during the budget period. As the amount involved in capital expenditure is usually high this requires careful attention of the top management. The budget is based upon the annual forecasts of capital expenditure of various divisions or departments. Each division or department of an organization sends the annual forecast of capital expenditure of its own department to capital expenditure sanction committee.

7. **Cash Budget:**

A cash budget is an estimate of cash receipts and disbursements during a future period of time. It precedes various other budgets like materials budgets and research and development budget. "The cash budget is analysis of flow of cash in a business over a future, short or long period of time. It is a forecast of expected cash intake and outlay.

The cash receipts from various sources are anticipated. The estimated cash collections for sales, debts, bills receivables, interests, dividends and other incomes and sale of investments and other assets will be taken into account. The amounts to be spent on purchase of materials, payment to creditors and meeting various other revenue and capital expenditure needs should be considered. Cash forecasts will include all possible sources from which cash will be received and the channels in which payments are to be made so that a consolidated cash position is determined.

The cash budget should be co-ordinate with other activities of the business. The functional budgets may be adjusted according to the cash budget. The available funds should be fruitfully used and the concern should not suffer for want of funds.

8. **Selling and distribution cost Budget**:

This budget includes all expenses relating to selling, advertising and distribution of goods. These expenses may be analyzed according to products, territories, salesman etc.. The fixed expenses under this category may be estimated on the basis of past experience and anticipated changes. Various selling and distribution overheads will vary with the anticipated sales figures. The responsibility for preparing this budget lies with the executives of sales departments.

9. Master Budget:

The master budget is the summary of various functional budgets. It is prepared by integrating various budgets into one consolidated budget so as to represent the budgeted profit and loss account and the budgeted balance sheet as at the end of the budget period.

In the words of Rowland and WilliumH.Harr, the master budget is, " a summary of the budget schedules in capsule from made for the purpose of presenting in one report the highlights of the budget forecast". The Institute of Management Accountants, London, defines it as, "the summary budget, incorporating its component functional budgets and which is finally approved, adopted and employed".

The master budget is prepared by the budget officer and requires the approval of the Budget committee before it is put into operation. This budget is used to co-ordinate the activities of various functional departments and also to serve as a control device.

The various steps involved in the preparation of this budget include the construction of (1) sales budget, as the starting point. (2) production budget (3) cost of production budget (4) cash budget and (5) the projected income statement and the balance sheet.

10. <u>Fixed Budget:</u>

The fixed budgets are prepared for a given level of activity, the budget is prepared before the beginning of the financial year. If the financial year starts in January then the budget will be prepared a month or two earlier, i.e. November or December. The changes in expenditure arising out of the anticipated changes will not be adjusted in the budget. There is a difference of about twelve months in the budgeted and actual figures.