BUDGETING AND BUDGETARY CONTROL

A budget is a financial statement, which is used to project the expected revenue, cost, assets, Liabilities and the cash flows.

It is normally prepared at the beginning of the accounting period to show the expected performance.

There are four types of budgets:

1. Functional budgets.
2. Cash budgets.
3. Flexible budget and fixed budget.
4. Master budget.

OBJECTIVES OF BUDGETARY CONTROLS

1. To communicate ideas and plans i.e. it is a way for managers to give orders to Subordinates or a two-way dialogue for exchange of ideas.
2. Co-ordinate activities.
3. Motivate employees this includes their performance through a system of feedback and performance evaluation.
4. Performance evaluation – Budgets acts as a basis of comparison where actual performance and budgeted performance can be evaluated for rewarding purposes.
5. Planning – Budgets force managers to think a head.
6. establishes a system of control – A budget is a standard against which actual performance is monitored.
7. To provide a framework for assigning responsibilities.
8. It is used as a measure of efficiency by comparing actual results with budgeted results.

PROBLEMS OF BUDGETARY CONTROLS

1. Its a costly exercise – Budgets needs research and forecasting where substantial cost will be incurred.
2. Budgets may set un- attainable targets this may be a source of frustration and demotivation.
3. Its a time consuming exercise – Feedback analysis, reporting etc. involves a lot of time which could be used in a more productive way.
4. Budgets are based on forecast and the parameters forecasted may not actually occur making budget irrelevant.
5. Rigidity – Budgets may be implemented as proposed without considering and incorporating expected changes.
6. Negative behavior complication – it arises where top management, which may cause subordinate to resist, imposes budgets.

STEPS IN BUDGET PREPARATION

1. Set plans – This involves establishment of objectives policy formation and strategies to achieve a given plan. Plan will dictate what budget need to achieve.
2. Set a budget period – This is the period, which will be covered by the budget. Period will be determined by what budgets need to achieve. Period could be a month, a quarter a year or a year.

a) Budget manual preparation – It's a document of instruction and responsibilities Governing persons preparing budgets. It is a guide on budget preparation. The content of a

Budget preparation manual includes:

a. Objective of budgetary planning and control.
b. Various stages of budgeting process and their control.
c. Organization charts to show how the organization is managed i.e. the level of authority.
d. Budget timetable.
e. Membership of Budget committee. f.
Charts of accounts.
g. Orders in which budgets will be prepared.

3. Budgets committee formation – It's the coordinating body in preparation and Administration of budgets. It manages the entire budgeting process by:

a) Issue of budget timetable
b) Allocation of responsibilities of budget allocation c)
P r o v i s i o n of information needed in budgeting
d) Communication of final budgets to appropriate managers e)
P e r f o r m a n c e evaluation and feedback provision
f) Continuous assessment of budgets

4. Identify principle budget factors – A budget factor it is a resource that limits the activity of the organization it may include: sales demand restrictions, machine hour's restrictions, and availability of cash.
5. Budget preparation – Once a limiting factor is identified the budgets should be prepared. A system should be adopted where subordinates are involved to reduce resistance.
6. Feedback mechanism – A budgets is used for performance evaluation as a way of communicating information for evaluation needs.

Functional budgets

These are budgets prepared by different departments in an organization. Each department is expected to draft the budget that is then forwarded to the top management for approval. These budgets include: sales budget, productions budget, material cost budget and labor cost budget.

Example 1

CPA JUNE 2004 Q4

Ideal products limited manufacturers two products A and B for the year ended 30 June 2004 the following information was assembled for preparation of budget.

Standard data per unit

	Standard price per kg Sh.	Product A per (kg) kg	Product B (kg) Kg
Direct Material			
M1	10	10	4
M2	20	4	6
Direct Labour	Standard rate per hour	Hours	Hours
L1	30	8	10
L2	20	12	5

The following additional information was available:

1. Fixed production overhead costs were recovered on a direct labor basis.
2. Administration, selling and distribution costs were absorbed at the rate of 20% of production cost.
3. Profit was estimated at the rate of 25% of cost of making and selling the product
4.

	Product A Sh. "000"	**Product B "000"**
Expected Sales for the year	13494	18816

5. Finished goods stock valued at standard production cost was as follows:

	Product A Sh. "000"	Product B "000"
1 July 2003	1730	1176
30 June 2004	1038	1568

6. Direct materials stock valued at standard prices was as follows

	Material M1 Sh. "000"	**Material M2 "000"**
1 July 2003	640	600
30th June 2004	360	800

7. For the year ended 30 June 2004 fixed overheads had been budgeted at sh. 5,760,000 and direct labor hours budgeted at 3,600,000 hours.

8. Its management expectation that there will be no opening or closing work in progress.

Required:

a) Production budget in units
b) Direct material cost budget
c) Purchase budget
d) Direct cost budget

Solution

Production budget in units = Sales in units + Closing stock in units – Opening stock in units

Selling price per unit = Cost per unit + profit per unit

	A		B
D. Material M1 10*10	100	4*10	40
M2 4*20	80	6*20	120
Direct Labour L1 8*30	240	10*30	300
L2 12*20	240	5*20	100
Fixed overheads 1.6*20	32	1.6*15	24
	692		584
Admin selling & dist. 20%	138.4		116.8
Cost of making & selling	830.4		700.8
Profit 25%	207.6		175.2
Sales	1038		876

Sales in units

A = $\frac{13494000}{1038}$ = 13000

B = $\frac{18816000}{876}$ = 21479.45

Opening stock in units.

A = $\frac{1730,000}{692}$ = 2500 B = $\frac{1568000}{584}$ = 2013.7

Closing stock in units

A = 1038000 / 692 = 1500 B = 1568000 = 2684.9 / 584 = 2684.9

(a)

Production Budget

	A	B
Sales in Units	13000	21479
Add : Closing stock in units	1500	2685
Less: Opening Stock in units	(2500)	(2014)
	12000	22150

(b)

Direct Material cost Budget

	M1	M2
A 12000*10*10 =	1200000	12000*4*20 = 960000
B 22150*4*10 =	88600	22150*6*20 = 2658000
Material used	2086000	3618000

(c) Purchases Budget = Materials used in production + Closing stock Raw Materials – opening stock Raw materials

	M1	**M2**
Materials used in production	2086000	3618000
Add: Closing stock raw material	360000	800,000
Less : opening stock raw material	(640,000)	(600,000)
	1806000	3818000

(d**) Direct Labour cost Budget**

	L1	**L2**
A 12000*8*30	= 2880000	12000*12*20 = 2880000
B 22150*10*30	= 6645000	22150*5*20 = 2215000
	9525000	5095000

Example 2

CPA: **June 2011 Q3**

Budget Period: it's the period defined by the management or by statutory requirements that a budget covers. It can be monthly, quarterly, semiannually or annually.

Budget Manual – it is a document prepared by the management accountant describing the objectives and procedures involved in the budget process and provide a useful source of information for the managers responsible for the budget preparation. It includes the timetable for the budget events and it should be circulated to all individuals responsible for preparing the budgets.

(b) Production budget = Sales in units + Closing stock in units – opening stock in units

	JUNE	JULY	AUGUST	SEPTEMBER
Sales	10800	15600	12200	10400
Add: Closing stock 25%	3900	3050	2600	2450
Less: opening stock	(2700)	(3900)	(3050)	(2600)
	12000	14750	11750	10250

(iv) Material P

	JUNE	JULY	AUGUST	SEPTEMBER
Material used in production	12000*4 = 48000	14750*4 =59000	11750*4= 47000	10250*4 = 4700

(iii**)** Material Q

	JUNE	JULY	AUGUST	SEPTEMBER
Material used in production	12000*5 = 60000	14750*5=73750	11750*5=58750	10250*5=51250

Example 3

CPA: MAY 2017 Q5b

Sales Budget = Revenue = units sold * selling price

= 10,000*2000 = ksh. 20,000,000

Production Quantity budget = Sales units +closing stock units – opening stock units

	units
Sales	10000
Closing stock 50% *4000	2000
Opening stock	(4000)
Productions	8000 units

Material usage budget

	X	**Y**
Production	8000	8000
	X	X
	5	3
	40,000kg	24,000kg

Material Purchase Budget

	X	y
Material used	**40,000**	**24,000**

Add: Closing Stock 125%16000	**20,000**	**125%x9600**	**12000**
Less: Opening Stock	**(1600)**		**(9600)**
Production	**44000kgs**		**26,400kgs**

Direct Labor Budget

	Production	**Finishing**
Production	8000	8000
	X	X
	4	2
	32000hrs	16000hrs
	X 100	X140
Total cost	3,200,000	2240,000

Budgeted income statement

	Ksh. "000"	Ksh. "000"
Sales Revenue		20,000
Cost of sales:		
Opening stock: 4000x1050	4200	
Production: 8000x1050	8400	
Closing stock: 2000x1050	(2100)	(10,500)
Gross profit		9500
Less: Expenses		
Selling administration and dist.		(5,500)
Net profit		4000

Master budget: This is a budget, which comprises of the cash budget, income statement and the balance sheet.

Example 1

The following is a balance sheet of Wote Ltd, as at 1 may 2015

	Cost	Depreciation	Net book value
Fixed Assets	sh. "000"	Sh. "000"	sh. "000"
Land and buildings	500,000	-	500,000
Machinery and equipment	124,000	84,500	39,500
Motor vehicles	42,000	16,400	25,600
	666000	100,900	565,100

Working capital:

Stock of raw materials (100 units)	4320
Stock of finished goods (110 units)	10450
Debtors:	
March sh. 7680	
April sh. 10,400	18080
Cash and bank	6790

	39640	
Less current liabilities		
Creditors	3,900	35740
Capital employed		600840
Represented by:		
500,000 ordinary shares (sh 1 each fully paid)		500000
Share premium		60000
Profit and loss		40480
		600840

The estimates for the next four months of the year 2015 were as follows:

	May	June	July	August
Sales ("ooo")	80	84	96	94
Production ("000" units)	70	75	90	90
Purchase of raw materials ("000" units)	80	80	85	85
Wages and variable overhead at sh. 65 per unit	4550	4875	5850	5850
Fixed overheads	1200	1200	1200	1200

a) The company intends to sell each unit for sh 219 and has estimated that it will have to pay sh.45 per unit for the raw materials. One unit of raw materials is needed to produce each unit of finished product.
b) All sales and purchases of raw materials are on credit. Debtor are allowed two months credit and suppliers of raw materials are paid in the month in which the purchases are incurred.
c) Cash from a loan secured on the land and buildings of sh. 120, 000 at an interest rate of 7.5% per annum is due to be received in June 2015. Machinery costing sh. 112,000. Will be received in May 2015 will be paid in August 2015 and the amounts is sh. 12,500

Depreciation for the four months including that on the new machinery is:

	Sh.
Machinery and equipment	15,733
Motor vehicles	3,500

The company uses FIFO method of stock valuation.

Required:

I. A cash budget for each of the four months.
II. Budgeted trading profit and loss and account for the four months to 31 August 2015.
III. Budgeted balance sheet as at 31 August 2015.

CASH BUDGET YEAR 2015 ("000")

	MAY	**JUNE**	**JULY**	**AUGUST**
Bal b/f	6790	5120	125845	132490
Receipts: From Debtors Loan	7680	10400 120,000	17520	18396
Total Receipt (a)	14470	135520	143365	150886
Payments:				
Creditors Wages and variable ohd	3600 4550	3600 4875	3825 5850	3825 5850

Fixed overhead Dividends Machinery	1200	1200	1200	1200 12500 112000
Total payments (b)	9350	9675	10875	135375
Bal c/d	**5120**	**125845**	**132490**	**15511**

Budgeted Income statement

Budgeted Sales	354@219		77526
Less Cost of sales:			
Opening stock finished goods	110@95	10450	
Add: Production (325 units)			
Opening stock raw materials	100(43.20+65)	10820	
Fresh materials (325-100)=225	225 (45+65)	24750	
Less: Closing stock finished goods	110+354-354=81 (45+65)	(8910)	(37110)
			40416
Less Expenses:			
Fixed overheads	1200x4		(4800)
Accrued interest			(2250)
Depreciation – equipment			(15733)
Motorvehicle			(3500)
Net profit for the period			14133
Retained profit bal. B/d			40840
Less: Dividend			(12500)
			42473

Budgeted balance sheet

Non-current Assets	**Cost**	**Accumulated depreciation**	**Net book value**
Land and buildings	500,000	-	500,000
Machinery and Equipment	236000	100233	135767
Motor vehicles	42000	19900	22100
Current Assets			657867
Stocks – raw materials	(100+330-325)x45	4725	
Fished goods stock	81x110	8910	
Debtors - July		21024	
August		20586	
Cash at bank		15511	70756
Financed by:			728623
Ordinary share capital			500,000
Share premium			60000
Retained profit			42473
Bank loan 7.5%			120000
Current Liabilities			
Creditors		3900	
Accrued interest		2250	6150
			728623

Example 2: December 2005 Q 1

Mavuno Ltd is a small-scale company that specializes in the production of farm tools

The company uses budgets for planning and controlling its activities. Currently the management are preparing budgets for the three months ending 31 March 2006
The projected balance sheet as at 31 December 2005 is shown below:

	Cost		**Depreciation**		**NBV**
Fixed Assets	2,000,000		200,000		1,800,000
Current assets					
Inventory			320,000		
Trade debtors			630,000		
Cash and bank balances			8400		
				958400	
Current liabilities					
Trade creditors	28,000				
Accrued expenses		20,000			
Proposed dividend		4000			
Taxes payables	3500		(55,500)		
902,900					
					2702900

Financed by:

Ordinary share capital	1000,000
Share premium	500,000
Retained profits	452,900
Long-term Liabilities	
Bank loan	750,000
	2702900

The following information has been extracted from the company's budget schedules:

	Sales Sh.	**Rent Sh.**	**Overheads Sh.**	**Wages Sh.**	**Material stocks sh**
2005					
November	500,000	80,000	180,000	40,000	272,000
December	340,000	80,000	180,000	60,000	320,000
2006					
January	400,000	80,000	190,000	60,000	480,000
February	600,000	80,000	200,000	80,000	464,000
March	580,000	80,000	200,000	74,000	464000
April	580,000	80,000	200,000	70,000	500,000

Additional information:

The company sells the farm tools at markup of 25%
Purchase of materials stocks is on credit and the company pays for it in the month of receipt
Employees are paid wages at the end of every week with the earnings of the last week of the month being settled in the following (Assume one month has 4 weeks)

1. Sales commission is paid one month in arrears at the rate of 1% of sales
2. Overheads include a monthly depreciation charge of sh. 25,000

3. 25% of the sales are on cash basis. The other 75% is receivable two months after the sale
4. The company will receive a loan of sh 2,500,000 in month of March 2006 from Wakulima Bank.
5. Old equipment will be sold for sh. 250,000 in February 2006 and new equipment will be purchased at sh. 1,200,000 to replace the old equipment sold. The new equipment will be paid for in the month of March 2006.
6. Rent is paid for quarterly in advance in the months of January, April, July and October

Required:

a) Cash budget for the three months ending 31 March 2006.
b) Budgeted trading profit and loss account for the three months ending 31 march 2006.
c) Budgeted balance sheet as at 31 March 2006.

CASH BUDGET

	JANUARY (SHS.)	FEBRUARY (SHS.)	MARCH (SHS.)
Bal b/f	8400	(472500)	(540500)
Cash sales 20%	100,000	150000	145000
Debtors 75%	375000	255000	300,000
Loan		-	2,500,000
Sale of asset		250,0000	-
Total receipts: (a)	483400	182500	2404500
Payments:			
Purchases	480,000	464000	464000
Overheads	165000	175000	175000
Rent	240,000	-	-
Equipment		-	1200000
	60000	75000	75500
Wages	3400	4000	6000
Sales commission	3500	-	-
Taxes	4000	-	-
Dividends	955900	718000	1925000
Total payments (b)	472500	(540500)	489000
Balance c/d (a – b)			

Determination of closing stock

Mark up	25/100	
Margin	25/125	
Gross profit	25/125x1580000 = 316000	
GP = sales – cost of sales		
Cost of sales = Sales –Gp	1580000-316000=1264000	
Cost of sales = opening stock +purchases – closing stock	1264000=264000	

Budgeted income statement

Sales (400+600+580)		1580000
Cost sales :		
Opening stock	320,000	
Add: purchases	1408000	
Less: Closing stock	(464000)	(1264000)
Gross profit		316000
Less: Expenses	240000	

Rent (80x3)	515000	
Overhead	75000	
Depreciation (25x3)	214000	
Wages	15800	(1059800)
Sales commission (4000+6000+5800)		(743800)
Net Loss		452900
Retained profit Bal b/d		(290900)
Net Loss		

Budgeted statement of financial position

Fixed Assets	2000000+1200000 – (200000+75000+250000	2675000
Current Assets		
Inventory		464000
Debtors (435+4500)		885000
Cash		489000
Total Asset		4513000
Equity and liability		
Ordinary share capital		1000000
Share premium		500000
Retained profit		(290900)
Noncurrent Liabilities		
Loan	(750,000 + 250 000)	3250000
Current Liabilities		
Creditors		28000
Accrued expenses	20000	
Wages	18500	
Commission	5800	
	(3400)	
	(15000 **)**	25900
		4513000

Example 3: CPA. : Dec 2009 Q1

	MAY	**JUNE**	**JULY**	**AUG**	**SEP**	**OCT**	**NOV**	**DEC**
	"000"	"000"	"000"	"000"	"000"	"000"	"000"	"000"
Sales units	4000	4200	4500	4600	4800	5000	3800	3000
sp	6000	6000	6000	6000	6000	8000	8000	8000
Sales revenue	24000	25200	27000	27600	28800	40000	30400	24000
Cash sales 50%	12000	12600	13500	13800	14400	20000	15200	12000
Credit Sales 50%	12000	12600	13500	13800	14400	20000	15200	12000
Cash from debtors	-	-	12000	12600	13500	13800	14400	20000
Wages & salaries	8000	8000	8000	10000	10000	10000	12000	12000
75%	6000	6000	6000	7500	7500	7500	9000	9000
25%	-	2000	2000	2000	2500	2500	2500	3000
	6000	8000	8000	9500	10000	10000	11500	12000

Cash Budget

	July	Aug	Sep	Oct	Nov	Dec
	"000"	"000"	"000"	"000"	"000"	"000"
Bal b/f	3000	1500	(1600)	15300	14100	8200
Receipt:						
Cash sales	13500	13800	14400	20000	15200	12000
Cash from debtor	12000	12600	13500	13800	14400	20000
Cash from shares			20000			
Total receipt (a)	28500	27900	46300	49100	43700	40200
Payments:						
purchases	12000	13000	14000	18000	16000	14000
Wages & Salaries	8000	9500	10000	10000	11500	12000
Overheads	7000	7000	7000	7000	8000	8000
Dividends						10000
Total payments (b)	27000	29500	31000	35000	35500	44000
Bal c/d	1500	(1600)	15300	14100	8200	(3800)

(b) Budgeted income statement

		Sh. "000"
Sales revenue		177800
Less: Cost of sales		
Opening stock	25000	
Add: purchases	86000	
Less: Closing stock	(38000)	(73000)
Gross profit		104800
Less : expenses:		
Wages & salaries	62000	
Overheads	45000	
Depreciation	8500	(115500)
Net Loss		(10700)
Profit & Loss bal. b/f		44600
Profit available for appropriation		33900
Less: dividends		10000
Retained earnings		23900

(c) Budgeted statement of financial position

	Cost	Depreciation	Net Book value
Fixed Assets			
(126000+30000)	156000	8500	147500
Current Assets			
Stock		38000	
Debtors		27200	65200
Total Assets			212700

Financed by:			
Share capital	100000+20000		120000
Retained earnings			23900
Current liabilities			
Trade creditors		24000	
Other creditors	(3000+8000+30000)	41000	
Bank overdraft		3800	68800
			212700

Cash budget: This is the budget which shows the cash flows expected by an organization. Non- cash items such as depreciation are normally excluded in the cash budget. Any activity which needs the payment in cash or any cash receipt must be taken into account. All transactions carried outside the budget period are excluded.

Example 1 – CPA MAY 2015 Q 5b

	April	**May**	**June**	**July**	**Aug**	**Sept**
Sales	360,000	350,000	440,000	350,000	360,000	360,000
Cash 20%x96%=19.2%	69120	67200	84480	67200	69120	69120
Cash 70%x97.5%=68.25%	245,700	238875	300300	238875	245700	245700
Credit 10%	-	36000	35000	44000	35000	36000
Sales Receipt				**350075**	**349820**	**350820**

Cash budget

	JULY	August	September
Opening balance	90,000	144575	171595
Receipt:			
Sales receipt	350075	349820	350820
Debentures		125000	
Total receipt	440075	619395	522415
Payments			
Payment of material	100,000	135000	90,000
Installation of machines		150000	-
Sales commission 0.03x350,000	10500	10800	10800
Dividends	-	-	100,000
Wages	100,000	72,000	54,000
Overheads	85000	80,000	72,000
Total payments	295500	447800	326800
Closing balance	144575	171595	195615

Example 2 – CPA MAY 2016Q4

DEBTORS COLLECTION SCHEDULE

	March	April	May	June	July	Aug
Sales	27000	33000	45000	55000	75000	50000
20% of sales	5400	6600	9000	11000	15000	10000
	21600	26400	36000	44000	60000	60000
Receipt 20%	4300	5280	7200	8800	12000	
65%		14040	17160	23400	28600	39000
15%			3240	3960	5400	6600
Collection						
	march	April	May	June	July	August
Cash	5400	6600	9000	11000	15000	
Debtors	4300	19320	27600	36160	46000	

Creditor payment schedule

Determination of purchases

Purchases = Cost of sales +Closing stock –Opening stock

	May	June	July	Aug
Sales	21000	28000	42000	22000
Closing stock	7000	10500	5500	
Opening stock	(5250)	(7000)	(10500)	
	22750	31500	37000	

Purchases schedule

	May	June	July
50% of purchases	11375	15750	15750
Debt	11100	11375	18500
Total payment	22475	27125	34250

Cash budget

	May	June	July
Opening Balance	8400	8400	15060
Cash from sales	9000	11000	15000

Cash from debtors	27600	36160	46000
Total Receipt	45000	55560	
Payments:			
Land	4300		
Dividend	-		1300
Overdraft	-	875	
Creditors	22475	27125	34250
Selling expenses	7000	8400	11200
Administrative expense	3700	4100	5100
Total payments	37475	40500	51850
Closing balance	7525	15060	24210
Overdraft	875		

FIXED AND FLEXIBLE BUDGETS.

A fixed budget – This budget is designed to remain unchanged irrespective of level of output.

Flexible budget – It's a budget designed to adjust according to the level of activity.

Example 1-CPA MAY 2002 Q4

Lamu Ltd produces a popular brand of biscuit, which sells under the brand name "Tamu" the biscuits are sold in packets of 100gm at sh. 20. To reduce the distribution cost the firm is only selling the product through the supermarket at sh. 12 per packet, the budgeted selling standard for the year ended December 2018 are given below:

	Shs.
Annual fixed manufacturing cost	500,000
Direct materials	2.50
Direct labor cost per hour	200
Variable factory overhead per hour	275,000
Selling cost (variable)	0.80
Output number of packets per hour	100
Number of working hours per week	40

At the end of the year, an analysis of the result revealed the following:

1. The actual cost was sh. 12.25 per unit
2. Direct material cost per packet reduced by 5%
3. The actual production rate was 98 packets per hour although there was no idle time
4. All units produced were sold
5. Actual fixed cost was sh. 480,0000
6. There was no change in selling and distribution cost per unit
7. Actual variable overheads amounted to sh. 550,000

Required:

1. The original/ static budget income statement for the year
2. Actual income statement for the year.
3. Flexible budget income statement for the year

Original / Static / fixed Budget income statement

	Sh. "000"	"000"
Sales Revenue : 100x40x52x12		2496
Less: production costs		
Direct Materials 100x40x52x2.5	520	
Direct Labour 40x52x200	416	
Variable overhead 40x52x275	572	

Annual fixed manufacturing cost	500	2008
Less: Expenses		
Gross profit		488
Selling costs 100x40x52x0.8		166.4
Net profit		321.6

Actual income Statement

	Sh. "000"	"000"
Sales Revenue : 98x40x52x12.75		2598.96
Less: production costs		
Direct Materials 98x40x52x2.375	484.12	
Direct Labour 40x52x200	416	
Variable overhead 40x52x200	550	
Annual fixed manufacturing cost	480	1930.12
Less: Expenses		
Gross profit		668.84
Selling costs 98x40x52x0.8		163.072
Net profit		505.768

Flexible budget

Activity Level = Actual / Budget x 100 = 98%

	"000"	"000"	Variance
Sales	98%x2496	2446.08	152.88F
Less: production costs			
Direct Material	98%x520	509.6	25.48F
Direct Labour	98%x416	407.68	8.32A
Variable factory ohds	98%x572	560.56	10.56F
Fixed overheads		500	20F
Gross profit		468.24	
Less Expenses			
Selling costs	98%x166.4	163.072	
Net profit		305.168	200.62F

Reconciliation statement

Actual net profit	505.768
Less: Favorable variances	(200.62)
Flexible budget profit	305.168

Example 2 -CPA - May 2005 Q4

a) State the objectives of budgetary planning and control systems.
b) Identify the limitations of using budgeting systems to regulate business activities.
c) Kaunda Limited manufactures one standard product. Currently it is operating at a normal level of activity of 70% with an output of 6,300 units, although the sales director believes that a realistic forecast for the next budget period would be at a level of activity of 50%.

Level of activity

	60%	70%	80%
Direct materials	37,800	44,100	50,400
Direct wages	16,200	18,900	21,600
Production overheads	37,600	41,200	44,800
Administration overheads	31,500	31,500	31,500
Selling and distribution overheads	42,300	44,100	45,500
Total cost	165,400	179,800	194,200

(c)

FLEXIBLE BUDGET @ 50%	
Direct Materials	31500
Direct Wages	13500
Production overheads (37600-3600)	34000
Administrative overheads	31500
Selling administration (42300-3600)	40500
Total cost	151000
Profit 1/4x151000	37750
Sales	188750

Example 3: CPA NOVEMBER 2010 Q 2

Breeze cottages Ltd a company operating in the hospitality industry is currently operation at 55 percent occupancy level. The information below relates to the financial year ended 30 September 2010.

Occupancy level	55%	75%	85%
	Sh.	Sh.	Sh.
Accommodation:			
Room cleaning costs	481800	657,000	744,600
Establishment costs	363,170	477,050	533,990
Sports facilities			
Recreational facilities costs	180675	246375	279225
Equipment costs	100,000	100,000	100,000

Additional information

a) The company's management expect all variable costs to increase by 3.5 per cent in the next financial year.
b) The management projects an occupancy level of 80% in the financial year due to expected favorable economic growth.
c) The company plans to upgrade its cottage to luxury standard in the next financial year. The fixed costs in relation to upgrading the rooms and sports equipment are expected to be sh. 50,000 and sh. 75,000 respectively.
d) It is the management policy to charge the cost of upgrading the rooms and the sports equipment against the profits of the next five years.

Required:

1. A flexed budget statement for the financial year ending 30 September 2011.
2. Assume the company's actual expenditure for this period ending 30 September 2011 is as follows:
   Room cleaning costs 727,560

Establishment costs	529258
Recreational facilities costs	275640
Equipment costs	190,000

Required:

I. Calculate the appropriate variances

II. For each variance in (b) above state two reasons which may contributed to their occurrence

(a) Flexible budget at 80%

Room cleaning costs	700800x3.5%	725328
Establishment cost	47050+28470	505520
Recreational facilities	262800x103.5%	271998
Equipment		100000
Upgrading costs: rooms Sports equipment		50000 75000
		1727846

(b)

	Actual	**Budget**	**Variance**
Room cleaning	727560	725328	2232A
Establishment costs	529258	505520	23728A
Recreational facilities	275640	271998	3642A
Equipment costs	190000	100000	90000A
Rooms	50000	50000	-
Sports	75000	75000	-
			119602A