**Budgeting**

***Topic Test***

|  |  |  |  |
| --- | --- | --- | --- |
| **Student Name:** | **SOLUTIONS!** | **CG:** |  |

**Time allowed:** 1 hour

**Material required/recommended for this assessment**

To be provided by the supervisor

This Question/Answer Booklet

To be provided by the candidate

*Standard Items:* Pens, pencils, eraser or correction fluid, ruler

*Special Items:* Non-programmable calculators satisfying the conditions set by the School

 Curriculum and Standards Authority for this course

**Marking Key**

|  |  |  |
| --- | --- | --- |
| Question | **Marks Allocated** | **Marks****Gained** |
| **Multiple Choice** | 5 |  |
| **6** | 15 |  |
| **7** | 25 |  |
| **8** | 10 |  |
| **Total** | **55** |  |

**Multiple Choice**

Each question has only one correct response. Signify your answer by circling the label (**a**, **b**, **c** or **d**) of the correct response. If you change your answer, completely erase your original answer. Questions where two or more responses are selected will score no marks.

1. If budgeted profit is greater than actual profit, the result is:

* 1. positive because actual income is greater than actual expenses.
	2. **negative because actual income is less than actual expenses.**
	3. positive because actual cash received is greater than cash paid.
	4. negative because actual cash received is less than cash paid.

2. Non-financial performance measures:

* 1. should not be used in a system to reward management performance
	2. are normally impossible to assess
	3. are seldom important in evaluating management performance
	4. **might include customer satisfaction, product quality and staff morale**

3. The master budget for a business:

* 1. is prepared by the firm’s senior management
	2. is distinct from the firm’s operational budgets
	3. includes all estimates except capital expenditure
	4. **consists of all the interrelated financial and operating budgets**

**Marvel Limited** has produced the following cash budget for the period July to September 2021:

|  |  |
| --- | --- |
|  | **$** |
| Cash balance at 30 June 2021 | 45,000 |
| *Estimated Receipts* |  |
| Receipts from customers | 860,000 |
| Proceeds from sale of assets | 35,000 |
| **Total cash available** | 940,000 |
| *Estimated Payments* |  |
| Payments to suppliers | 705,000 |
| Purchase of assets | 120,000 |
| General expenses | 50,000 |
| Interest on loan | 5,000 |
| Repayment of loan | 45,000 |
| **Total payments** | 925,000 |
| Cash balance at 30 September 2021 | 15,000 |
|  |  |

4. Based on the information above, which of the following statements is true?

1. **Marvel Limited will not need to arrange an overdraft during the budget period**
2. The business is expected to be profitable during the budget period
3. The business will make a loss on the sale of assets
4. All of the above are true

5. Of the items listed in the cash budget above, which two items will also appear in the Budgeted Income Statement?

1. Receipts from customers and payments to suppliers
2. **Interest on loan and general expenses**
3. Interest on loan and repayment of loan
4. Proceeds from sale of assets and purchase of assets

**✓ 1 mark each ( /5 marks)**

**Application Questions**

1. The following information has been provided by the owner of **Sector 7 Enterprises**:

The business’s opening cash balance at 1 May 2017 is $9,000. Over the next three months the business expects to have monthly wages of $3,000 and monthly office expenses of $700. The June quarterly bills will be utilities costs of $1,500 and rent of $6,000.

The business is planning to purchase a new computer for $5,500 cash on 1 June and this is to be depreciated at 35% pa straight line.

Sales at the beginning of the year were as follows:

* January $13,000
* February $12,000
* March $15,000
* April $ 8,000

Estimated sales are $12,000 per month. Analysis of the results from the beginning of the year has revealed that 60% of sales are for cash. Of the credit sales, 50% are paid the month following sale, 30% two months after sale and the remainder in the third month after sale.

Inventory purchases are made on credit and are paid for the month after. This attracts a 3% discount. In the first four months of the year $6,000 was purchased each month.

Estimated purchases for the next three months are as follows:

* May $ 8,000
* June $12,000
* July $ 9,000

**Workings**

**Creditors Schedule**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Month** | **May** | **June** | **July** | **Disc Rec** |
| April ($6000) | 5,820  | - | - | 180 |
| May ($8000) | - | 7,760  | - | 240 |
| June ($12000) | - | - | 11,640  | 360 |
|  | $5,820 | $7,760 | $11,640 | $780 |

6. cont

*You are required to:*

1. Prepare a Schedule of Collections from Debtors for the business for the quarter ending 31 July 2017

**Schedule of Collections from Debtors**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Month** | **Cr Sales** | **May** | **June** | **July** |
| February | 4800 | 960 20 | - | - |
| March | 6000 | 1,800 30 | 1,200 20 | - |
| April | 3200 | 1,600 50 | 960 30 | 640 20 |
| May | 4800 | - |  2,400 50 | 1,440 30 |
| June | 4800 | - | - | 2,400 50 |
|  |  | $4,360**✓** | $4,560**✓** | $4,480**✓** |

**✓ 1 mark each ( /3 marks)**

6. cont

1. Prepare a simple Cash Budget for the business, showing separately the months of May, June and July 2017

**Sector 7 Enterprises**

**Cash Budget**

**For quarter ending 31 July 2017**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **May** | **June** | **July** |
| Opening Cash balance  | 9,000 **✓** | 11,040 | (1,660) |
| *Add* **Estimated Receipts** |  |  |  |
| Cash sales | 7,200  | 7,200  | 7,200 **✓✓** |
| Collections from debtors | 4,360  | 4,560  | 4,480 **✓** |
| **Total Cash Available** | 20,560 | 22,800 | 10,020 |
|  |  |  |  |
| *Less* **Estimated Payments** |  |  |  |
| Payments to creditors | 5,820**✓** | 7,760**✓** | 11,640 **✓** |
| Wages | 3,000 | 3,000 | 3,000 **✓** |
| Office expenses | 700 | 700 | 700 **✓** |
| Utilities |  | 1,500 **✓** |  |
| Rent |  | 6,000 **✓**  |  |
| New computer |  | 5,500 **✓** |  |
| **Total Payments** | 9,520 | 24,460 | 15,340 |
| Ending Cash balance  | $11,040 | $(1,660) | $(5,320) |
|  |  |  |  |

**✓ 1 mark each ( /12 marks)**

7. **Donald Quarries** is a large earthmoving and soil supplies contractor operating in the hills near Perth. The firm has a regular cash budgeting system in place and the General Manager is suggesting that it might be a good idea to prepare a Budgeted Income Statement as well. Use the Cash Budget given below for the next three months and the additional information to answer the following questions:

**Donald Quarries**

**Cash Budget for the 3 months October – December 2021**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **OCTOBER** | **NOVEMBER** | **DECEMBER** |
| Opening balance | 17 600 | 142 600 | 6 600 |
| **Receipts**Accounts receivable | 221 000 | 240 000 | 235 000 |
| Proceeds of sale of shares |  | 20 000 |  |
| Total cash available | 238 600 | 402 600 | 241 600 |
| **Payments**Fuel | 15 000 | 19 000 | 17 000 |
| Wages | 55 000 | 75 000 | 65 000 |
| Interest payment |  |  | 6 000 |
| Loan repayment |  |  | 100 000 |
| Purchase of truck |  | 250 000 |  |
| Electricity payment | 24 000 |  |  |
| Other cash expenses | 18 000 | 20 000 | 20 000 |
| Owners’ drawings | 8 000 | 8 000 | 8 000 |
| Total estimated payments  | 96 000 | 396 000 | 285 000 |
| Budgeted closing balance | 142 600 | 6 600 | (43 400) |

**Additional information**

* Fees and sales are all on credit and collected in the month following the service or sale. Fees/sales for December are estimated to be $220 000.
* Electricity accrued in December is anticipated to be $525.
* The purchase price of the shares was $25 000.
* All business assets are predicted to depreciated at a rate of $18 000 per month.
* The annual insurance premium of $84 000 was paid on 1/7/21.
* Interest is accrued and paid quarterly.
* All other expenses included in the cash budget are paid in the month to which they relate.

**WORKINGS:**

Fees/sales: 220000 + 240000 + 235000 = 695000

 Fuel: 15000 + 19000 + 17000 = 51000

Wages: 55000 + 75000 + 65000 = 195000

Electricity: 24000 + 525 = 24525

Loss on sale of shares: 20000 - 25000 = 5000

Other cash expenses: 18000 + 20000 + 20000 = 58000

Depreciation: 18000 x 3 = 54000

Insurance: 84000/12 = 7000 x 3 = 21000

**DONALD QUARRIES**

**BUDGETED PROFIT & LOSS STATEMENT FOR 3 MONTHS ENDING 31/12/21**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **$** | **$** |  |
| **Revenue** |  |  |  |
| **Income** |  |  |  |
| Fees/sales |  | 695 000 | **✓✓** |
| Less**: Estimated expenses** |  |  |  |
| Fuel | 51 000 |  | **✓** |
| Wages | 195 000 |  | **✓** |
| Electricity | 24 525 |  | **✓✓** |
| Interest |  6 000 |  | **✓** |
| Loss on sale of shares | 5 000 |  | **✓✓✓** |
| Other cash expenses | 58 000 |  | **✓** |
| Depreciation | 54 000 |  | **✓✓** |
| Insurance | 21 000 | 414 525 | **✓✓✓** |
| Budgeted Profit |  | 280 475 | **✓** |

*Minus one mark for each item incorrectly included*  **( /17 Marks)**

(b) Explain the purpose of budgets and the benefits that a business like Donald Quarries might expect from them.

The object of budgets is planning and setting targets so that problems can be anticipated

 and the business’s performance can be evaluated. **✓**

In this example, the cash budget is forecasting an overdraft of $43 000 but a profit of $275 475 by the end of December and so the business can make arrangements to either avoid this (perhaps by delaying the payment for the new truck) **✓** or varying the loan repayment. **✓**

Actual and budgeted performance can be compared to identify problem areas, and management can be motivated to improve their performance. **✓**

**✓ 1 mark each ( /4 marks)**

(c) At the executive level, planning decisions about products and services are made that may include product *cost leadership* or product *differentiation* strategies.

Explain the difference between these two strategies.

**Cost leadership** is a strategy to position a business as being price sensitive. **✓** It involves a systematic process to eliminate waste and inefficiencies and lower purchasing costs. This will enable the business to sell products more cheaply than its competitors. **✓**

The **differentiation** strategy is about positioning the business so that it is recognised as providing a good or service that is distinct from competing products. **✓** The product itself does not need to be unique but some aspect of it should be exclusive or distinct. **✓**

**✓ 1 mark each ( /4 marks)**

8. **Polaris Traders** provides you with the following Performance Report.

**Polaris Traders**

**Budgeted Income Statement Performance Report**

**For year ended 30 June 2014**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Budgeted | Actual | Variance |
| Sales | 796,000 | 752,000 | 44,000 U**✓** |
| Cost of sales | 469,500 | 436,500 | 33,000 F**✓** |
| **Gross Profit** | 326,500 | 315,500 | 11,000 U**✓** |
|  |  |  |  |
| **Operating Expenses** |  |  |  |
| Wages | 144,000 | 147,600 | 3,600 U**✓** |
| Other expenses | 105,000 | 105,000 | - |
| Interest | 5,000 | 5,000 | - |
| Insurance | 7,500 | 7,500 | - |
| Depreciation | 8,500 | 8,500 | - |
| **Total expenses** | 270,000 | 273,600 | 3,600 U  |
| **Profit for the period** | $56,500 | $41,900 | 14,600 U **✓** |

*Required:*

1. Complete the **variance** column in the Performance Report.

**✓ 1 mark each ( /5 marks)**

8. cont

1. Comment on the results of the Performance Report prepared above.

The business predicted a profit of $56,500, but the actual profit was $14,600 less at $41,900. **✓**

The main factors that contributed to this downturn were:

* lower than expected sales – down $44,000
* this lead to a lower than expected gross profit – down $11,000
* wages were higher than expected - $3,600

**✓✓ any two (2) factors**

To improve their profit performance they should investigate:

* the drop in sales and perhaps consider an advertising campaign to boost sales
* the increase in wages and perhaps consider the staff needs for the business more closely

**✓✓ any two (2) reasonable recommendations**

**✓ 1 mark each ( /5 marks)**

**End of Topic Test!**