

Management Accounting:

Level 4:
Unit 5

Lecturer: Matthew Smith-Barrett

Unit Content: (Syllabus)

Level 4:
Unit 5

On successful completion of this unit a student will be able to:

- Demonstrate an understanding of Management Accounting Systems.
- Apply a range of management accounting techniques
- Explain the use of planning tools used in management accounting
- Compare ways in which organizations could use management accounting to respond to financial problems.

Learning Outcome 3:

Level 4:
Unit 5

Upon completion of this Learning Outcome, students should:

- Explain the use of planning tools used in management accounting

P.4 Explain the advantages and disadvantages of different types of planning tools used for budgetary control.

M.2 Analyse the use of different planning tools and their application for preparing and forecasting budgets.

D.3 Evaluate how planning tools for accounting respond appropriately to solving financial problems to lead organizations to sustainable success.

Week 7 - Use Budgets for Planning and Control:

Level 4:
Unit 5

Assessment Criteria P3, M3 & D3:

Upon completion of this lesson, students will be able to:

- Use Budgets for Planning and Control:
 - Preparing a budget.
 - Different types of budgets (e.g. capital and operating)
 - Alternative methods of budgeting
 - Behavioural implications of budgets
- Pricing:
 - Pricing strategies
 - How do competitors determine their prices?
 - Supply and demand considerations.

Week 7 -
Use budgets for planning
and control:

Level 4:
Unit 5

Management Accounting
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Introduction: Budgeting

L.O. 3:
P3

A **budget** is a quantitative expression of a plan for a defined period of time. It may include planned sales volumes and revenues, resource quantities, costs and expenses, assets, liabilities and cash flows. It expresses strategic plans of business units, organizations, activities or events in measurable terms. (Chartered Institute of Management Accountants 2016)

A budget is the sum of money allocated for a particular purpose and the summary of intended expenditures along with proposals for how to meet them

Purpose of a Budget

L.O. 3:
P3

Budget helps to aid the planning of actual operations by forcing managers to consider how the conditions might change and what steps should be taken now and by encouraging managers to consider problems before they arise. It also helps co-ordinate the activities of the organization by compelling managers to examine relationships between their own operation and those of other departments.

Purpose of a Budget (cont'd)

L.O. 3:
P3

Other essentials of budgeting include:

- To control resources
- To communicate plans to various responsibility center managers.
- To motivate managers to strive to achieve budget goals.
- To evaluate the performance of managers
- To provide visibility into the company's performance
- For accountability

How Budgets link with strategic plans and objectives

L.O. 3:
P3

- It is vital that businesses develop plans for the future. Whatever a business is trying to achieve, it is unlikely to come about unless its managers are clear what the future direction of the business is going to be.
- The budget(s) set out, in detail, the short-term plans and targets necessary to fulfil the strategic objectives

Periodic and continual budgets

L.O. 3:
P3

Budgeting can be undertaken on a periodic or a continual basis.

A **periodic budget** is prepared for a particular period (usually one year). Managers will agree the budget for the year and then allow the budget to run its course.

A **continual budget**, as the name suggests, is continually updated. We have seen that an annual budget will normally be broken down into smaller time intervals (usually monthly periods) to help control the activities of a business.

Benefits of Budgeting

L.O. 3:
P3

- Financial Control
- Goal setting
- Financial Awareness
- Organization of Expenditure and Income

How Budgets help managers

L.O. 3:
P3

1. Budgets tend to promote forward thinking and possible identification of short term problems
2. Budgets can be used to help coordination between the various sections of the business
3. Budgets can motivate managers to better performance
4. Budgets can provide a basis for system of control

Budgets as a planning tool

L.O. 3:
P3

Budgets tend to promote forward thinking and possible identification of short term problems: -

- Identifying potential problems early gives managers time for calm and rational consideration of the best way of overcoming it. The best solution to the potential problem may only be feasible if action can be taken well in advance.
- Discovering problems in a good time can leave a number of means of overcoming the problem open to exploration.

Budgets as a coordination tool

L.O. 3:
P3

Budgets can be used to help coordination between the various sections of the business

- It is crucially important that the activities of the various departments and sections of the business are linked so that the activities of one are complementary to those of another. For example, the activities of the purchasing/procurement department of a manufacturing business should dovetail with the raw materials needs of the production departments.

Budgets as a motivation tool

L.O. 3:
P3

Budgets can motivate managers to better performance

- Managers will be better motivated by being able to relate their particular role in the business to its overall objectives. Since budgets are directly derived from strategic objectives, budgeting makes this possible.

Budgets as a control tool

L.O. 3:
P3

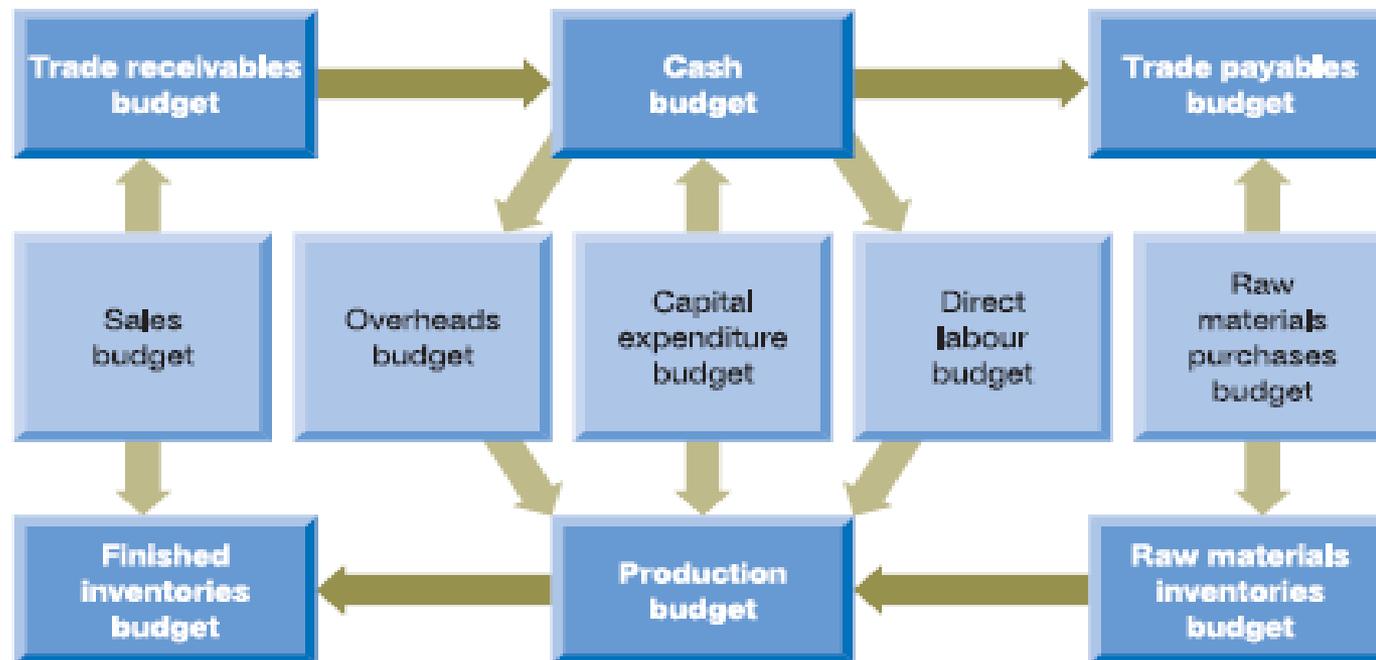
Budgets can provide a basis for system of control

- Budgets are financial plans. This means that, if actual performance can be compared with the budget (plan) for each aspect of the business, divergences from plan can be spotted. Steps can then be taken to bring matters back under control where they are going out of control.

How budgets link to each other

L.O. 3:
P3

Figure 6.2 The interrelationship of various budgets



This shows the interrelationship of budgets for a manufacturing business. The starting point is usually the sales budget. The expected level of sales normally defines the overall level of activity for the business, and the other operating budgets will be drawn up in accordance with this. Thus, the sales budget will largely define the finished inventories requirements, and from this we can define the production requirements and so on.

Budget Types

L.O. 3:
P3

- Sales Budget
- Production Budget
- Capital Budget
- Cash flow / Cash Budget
- Marketing Budget
- Project Budget
- Revenue Budget
- Expenditure Budget

Conclusion:

L.O. 3:
P3

Reference List

L.O. 2:
A.C. 2.1

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