

# **Grade 12 Accounting**

## **Projected Income Statement and Cash Budget**

# BUDGETING

- In grade 11 you learned to prepare and present a Cash Budget and Projected Income Statement for a sole trader
- This year the focus will be on the:
  - 👉 **analysis**
  - 👉 **interpretation** and
  - 👉 **comparison**of Cash budgets and Projected Income Statements for both sole traders and companies



# Budget period and classification

## 1. Budget period

- Budgets can be prepared for a **month, three months, six months**, a **year** or even for a **number of years**.
- The **period of time** over which the budget is drawn up is called the **budget period**.
- Budgets generally cover one of three periods of time:
  - **Short-term budget** – usually **less** than one year
  - **Medium-term budget** – usually **one year**
  - **Long-term budget** – usually prepared for a **number of years**

## 2. Budget classification

- Budgets are normally classified into two main groups namely



### Operating budget:

- \* relate to the **income and expenses** of a business
- \* these budgets include the **sales budget, cost of sales budget** and **operating expense budget**
- \* are used to **plan** the **incomes and expenses**
- \* are combined to form part of the **Projected Income Statement**



**Financial budget:**

- \* relate to the **assets and liabilities** of a business
- \* these budgets include the **cash budget, capital budget** as well as the budgets for **debtors, creditors** and **inventory**
- \* are combined to form part of the **Budgeted Balance Sheet**

# Reasons for budgeting

There are a **number of reasons** why budgeting is such an important and valuable business tool and there are several ways in which a business benefits from having an effective budgeting process

## 1. Planning

- Planning is the **primary purpose** of budgeting
- Once the budget is completed it should provide the business with a **financial plan**
- This financial plan sets the **course** that needs to be followed and the **actions** that need to be taken in order to **achieve the goals** of the business

## 2. Internal control

- Budgets provides management with an effective tool that can be used to **monitor and control** the activities of the business
- Budgets are used by management to ensure that
  - \* the **plans** of the business are **followed**
  - \* **cash-flow** problems are **avoided**
  - \* **expenditure** is kept **under control**
  - \* **budget targets** and **business objectives** are **achieved**
- Management will perform regular comparisons between the **actual results** and the **budgeted figures**.
- From theses comparisons, management can **identify potential problem areas**

- Where there are **significant differences** between actual and budgeted figures, management will conduct **further investigations** to establish the **reasons** for the deviations
- Based on their findings, management will either:
  - **take corrective action**
  - **modify business operations**
  - Implement **control measures** to **prevent** similar problems from happening in the future
- Deviations can be as a result of:
  - the **budgeted figures** being **unrealistic** (over or under budgeted) or
  - **circumstances having changed**management will **make adjustments** to correct the budget
- Budgets can also be used to **control spending** by using the budget amounts as **set fixed limits**



### 3. Communication and co-ordination

- The budgeting process help to ensures that there is **good communications** and co-ordination within a business.
- Budgets allow management to **communicate their expectations** and **convey the business's objectives**

### 4. Motivation and evaluations

- The budgeting process can help to **motivate employees**. Employees who are involved in creating and setting their own budgets, will be more likely to strive to achieve the objectives of those budgets
- Budgets may be used to **motivate employees** by setting **performance targets** based on the budget

## Important concepts

- ❖ **Cash budget** – A forecast of **cash receipts** and **cash payments**
- ❖ **Projected Income Statement** – A forecast of **income** and **expense**
- ❖ **Debtors' collection schedule** – A schedule (plan) of how the business will **collect** money from its debtors
- ❖ **Creditors' payment schedule** – A schedule (plan) of how the business will **pay** its creditors

# Sales

- ❑ The **main source of income** for a business is **sales**
- ❑ Sales can be for **cash** or on **credit**
- ❑ **Cash sales** are received **immediately** and will be entered as a **receipt** in the cash budget **in the month of sale**
- ❑ **Credit sales**: the money from credit sales **will be collected** from debtors in the **future**
- ❑ **Cash and credit sales** may need to be **calculated** from **given information**

## Debtors' collection schedule

Use the following steps when preparing a debtors' collection schedule:

- 1) Calculate and enter the **CREDIT SALES**
- 2) Take each month and indicate the **PERCENTAGE** that will be received in that month
- 3) Do the **calculations** – using the **credit sales** and the **percentage** to calculate the **AMOUNT TO BE RECEIVED** from the debtors
- 4) **TOTAL THE COLUMNS** for each month

## Example – Debtors' collection

Prepare the debtors' collection schedule for **July, August and September 2019** from the information below:

- i) 60% of sales are for cash
- ii) Debtors are expected to pay as follows:
  - 50% in the same month as the transaction subject to a 10% discount
  - 30% in the month following the credit sales transaction month
  - 17% in the second month following the credit sales transaction month
  - 3% is expected to be written off
- iii) Total sales:

June – R160 000	July – R150 000
August – R180 000	September – R200 000

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iii) Total sales:

June – R160 000

July – R150 000

**August – R180 000**

September – R200 000

Step 1: Determine credit sales

(Credit sales = 40%)

	Credit sales	July	August	September
June	160 000 x 40/100 = 64 000			
July	150 000 x 40/100 = 60 000			
August	180 000 x 40/100 = 72 000			
September				



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*Step 2: Indicate the percentage that will be received*

June      July      August      September

	Credit sales	July		August		September	
June	64 000	30		17			
July	60 000						
August	72 000						
September	80 000						

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Step 3: Do the calculations of the amounts to be received

	Credit sales	July		August		September	
June	64 000	30	$(64\ 000 \times 30/100) = 19\ 200$	17	$(64\ 000 \times 17/100) = 10\ 880$		
July	60 000						
Aug	72 000						
Sep	80 000						

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June	64 000	30	19 200	17	10 880		
July	60 000	50-10	$(60\ 000 \times 50/100)$ $= 30\ 000 - 10\%$ $= 27\ 000$	30	$(60\ 000 \times 30/100)$ $= 18\ 000$	17	$(60\ 000 \times 17/100)$ $= 10\ 200$
Aug	72 000			50-10		30	
Sep	80 000					50-10	

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June	64 000	30	19 200	17	10 880		
July	60 000	50-10	27 000	30	18 000	17	10 200
Aug	72 000			50-10	(72 000 x 50/100) = 36 000 – 10% = 32 400	30	(72 000 x 30/100) = 21 600
Sep	80 000						

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July	60 000	50-10	27 000	30	18 000	17	10 200
Aug	72 000			50-10	32 400	30	21 600
Sep	80 000					50-10	(80 000 x 50/100) = 40 000 – 10% = 36 000



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July	60 000	50	27 000	30	18 000	17	10 200
Aug	72 000			50	32 400	30	21 600
Sep	80 000					50	36 000
			<b>46 200</b>		<b>61 280</b>		<b>67 800</b>



## Creditors' payment schedule (Creditors' budget)

The following must be considered when the Creditors' budget is calculated:

- 1) **When and how much stock** is purchased on credit
- 2) Remember we have payment to creditors because we **BOUGHT**
- 3) **When** is the payment **due**?

## Purchases

- ❑ A business needs to **buy stock** to be able to have sales
- ❑ Purchasing of stock can be for **cash** or on **credit**
- ❑ **Cash purchases** are paid **immediately** and will be entered as a **payment** in the cash budget **in the month of purchase**
- ❑ **Credit purchases**: the money for credit purchases **will be paid** to creditors in the **future** (normally the next month)
- ❑ **Cash and credit purchases** may need to be **calculated** from **given information**

- If a **constant stock level** is maintained then purchases will not be given to you.
- You must then remember

**Purchases = Cost of sales**

## Example Creditors' payment

Calculate the expected payments to creditors for credit purchases for the budget period January – March 2019

### Information

Creditors are paid in full in the month following the purchases

Actual <b>cash</b> purchases of stock	November 2018	R20 000
	December 2018	R22 000
Budgeted <b>cash</b> purchases of stock	January 2019	R20 000
	February 2019	R23 000
	March 2019	R24 500

Actual <b>credit</b> purchases of stock	November 2018	R14 000
	December 2018	R12 000
Budgeted <b>credit</b> purchases of stock	January 2019	R10 000
	February 2019	R11 000
	March 2019	R13 000

## Example Creditors' payment

Interpretation of the instruction that the creditors will be paid in full the following month:

Actual <b>credit</b> purchases of stock	November 2018	R14 000	This will be paid in December, however December is not part of the budget months
	December 2018	R12 000	Will be paid in January and forms part of the budget months
Budgeted <b>credit</b> purchases of stock	January 2019	R10 000	Will be paid in February and forms part of the budget months
	February 2019	R11 000	Will be paid in March and forms part of the budget months
	March 2019	R13 000	This will be paid in April. April is not part of the budget months

## Example Creditors' payment

So the months of December, January and February will be used

Actual <b>credit</b> purchases of stock	November 2018	R14 000	This will be paid in December, however December is not part of the budget months
	December 2018	R12 000 ✓	Will be paid in January and forms part of the budget months
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### Creditors payment schedule: January – March 2019

Month	Credit purchases	January	February	March
December	12 000	12 000		
January	10 000			
February	11 000			

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January	10 000		10 000	
February	11 000			11 000
		<b>12 000</b>	<b>10 000</b>	<b>11 000</b>

Actual <b>cash</b> purchases of stock	November 2018	R20 000
	December 2018	R22 000
Budgeted <b>cash</b> purchases of stock	January 2019	R20 000
	February 2019	R23 000
	March 2019	R24 500

Month	Credit purchases	January	February	March
December	12 000	12 000		
January	10 000		10 000	
February	11 000			11 000
		<b>12 000</b>	<b>10 000</b>	<b>11 000</b>

Extract from the Cash budget:

Cash Payments	January	February	March
Cash purchases	20 000	23 000	24 500
Payment to creditors	12 000	10 000	11 000

## How to prepare for this work:

- Make sure you can do the calculations
- Do lots of exercises to get familiar with the interpretation



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**THANK YOU**