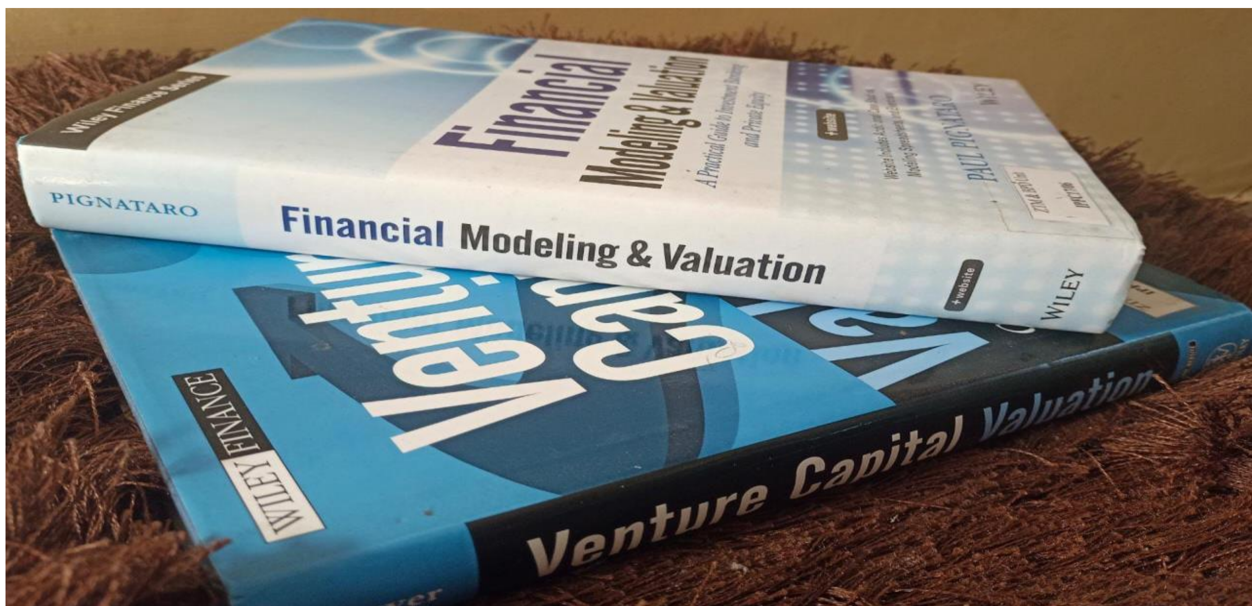
MOFPI

NIFTEM-K

PM Formalisation of
Micro food processing Enterprises Scheme

HANDBOOK
FOR
FINANCIAL MANAGEMENT



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Introduction:

PMFME is a centrally funded program that is implemented in close conjunction with the individual State Nodal Agencies. All States/UTs have designated Nodal Agencies for the scheme's implementation. The MIS portal for the PMFME Scheme is accepting individual applications for credit-linked subsidies for food processing unit upgradation. The Scheme is to be implemented for a period of five years from 2020-21 to 2024- 25 with an outlay of INR 10,000 Crore. The main theme of the Scheme is the One District One Product (ODOP) approach, a part of a broader strategy of concentrated agro and industrial development focused on each district.

The scheme is aimed to support capital investment for gradation and formalization with regulatory compliance, capacity building through imparting technical knowledge and skill training, handholding support for the preparation of DPR, availing bank loan and up gradation. It is also inclined to support to Individual Micro Enterprises in terms of credit-linked capital subsidy @35% of the eligible project cost with a maximum ceiling of Rs. 10 lakh Seed capital @ Rs. 40000/- per member of NHG for working capital and purchase of small tools would be provided under the scheme.

Under its component of capacity building, the scheme tries to ensure that every small business owner in the food processing sector shall be well aware of all the essential components of running a successful business. In this order, finance plays a very important part and it is necessary for an entrepreneur to understand financial management and its related dimensions.

‘Why should I become financially literate? I excel in my own field of expertise.’

As an entrepreneur you may be thinking of this statement before starting this module. An enterprise is all about time, effort and money of the founder. An understanding about the financial concepts will make you much more efficient with all the three determinants of entrepreneurial success. For example, you are a bakery products manufacturer and you have taken some debt from a bank. Now you need to manage your finances in such a manner so that the debt liability will reduce quickly. For this, you need to understand your costs, the activities which are costing you maximum so that you can plan for alternative sources to do

those activities. You also need to understand, basic accounting concepts so that you may take the best suited organizational form for your enterprise. Similarly, you need to understand varied techniques of inventory management and control in order to curtail your holding and reordering costs. You may appoint someone who can take care of all these matters but as an owner you should be aware of all the funds and cash inflows and outflows of your business so that you may take necessary action if any contingency arises.

Apart from this an understanding of financial management will aid in business planning, organization and control and leads to increased business efficiency. As you move up in your entrepreneurial career ladder, your enterprise will demand for your management and financial expertise more than your domain knowledge of bakery product manufacturing.

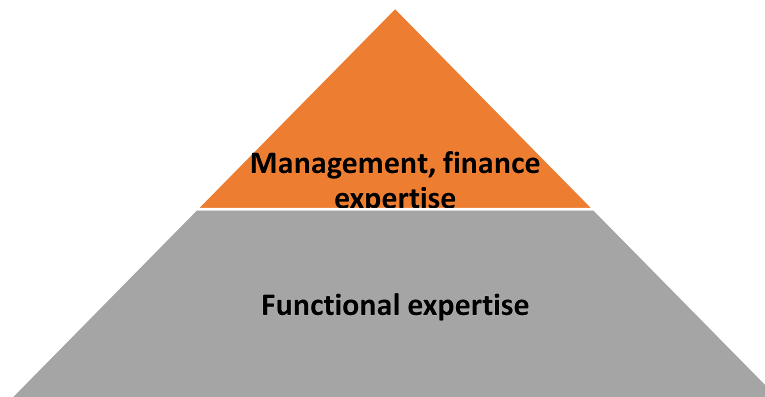


Figure 1: Expertise in firm's Hierarchy

So, lets get inside the module and understand financial management and accounting in the most simplest terms.

1. Introduction to Financial Management

Financial management is concerned with the acquisition and use of funds. Fundraising may include decisions about the cost of capital, capital structure, capital markets, IPOs, and so on. Fund utilization may include Capital Budgeting, Portfolio Management, Working Capital, Management, and other activities.

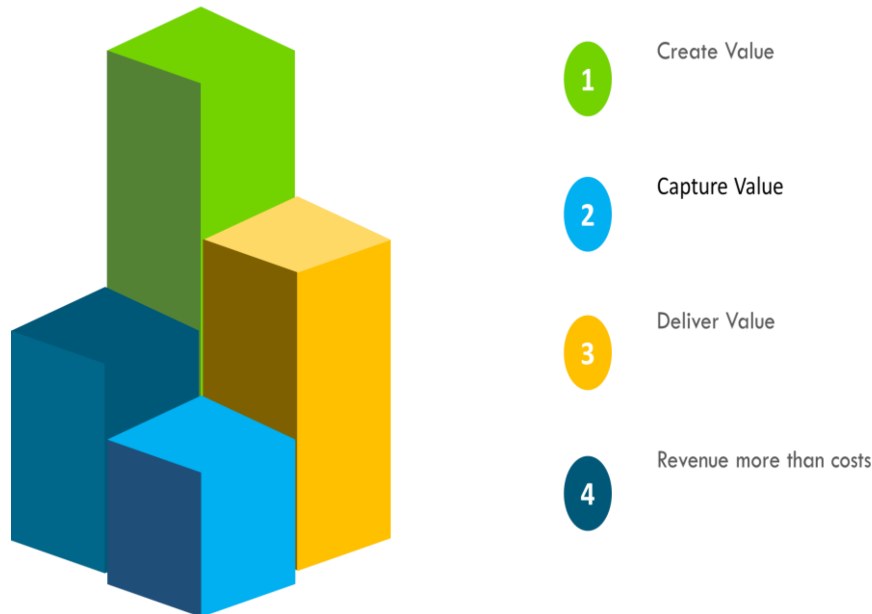


Figure 2: The basic business model

Every single aspect of running a company requires financial resources, whether it is production, customer service, or trade. When all is said and done, a business is considered to have made a "surplus" or "profit" when the entire amount of money received is greater than the total amount of money spent. If this is not the case, we refer to the financial state of the company as being in "deficit" or "loss." Every company has the same overarching objective: to make a profit. Because of this, the person or people who promoted the economic activity are always interested in learning the results of it.

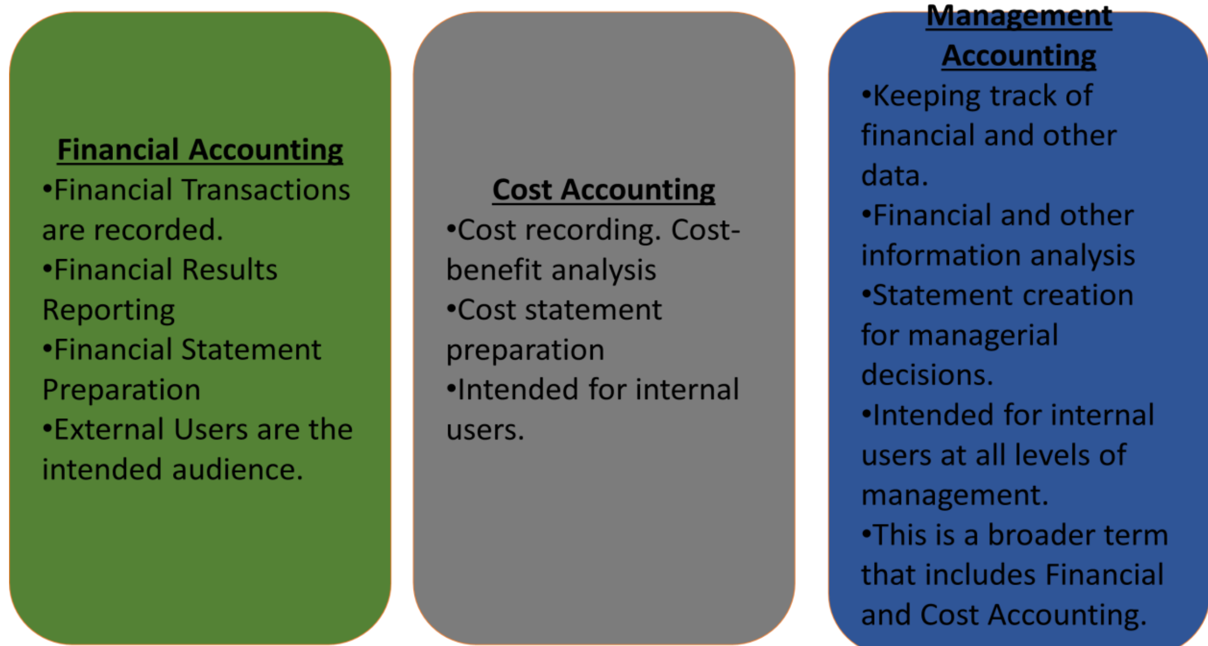
Throughout the course of running a firm, a number of transactions will take place. It is extremely unlikely that one could recall all of them. Because of this, a company is required to keep a record of all of these exchanges/ transactions in order to ascertain the results of the business activities. For the purpose of assisting the promoter in accurately recording all financial transaction and being aware of the results of business interactions, a systematic and rigorous science has been developed.

It has been described as the art & science of recording financial transactions in a systematic manner in order to indicate (a) the true financial condition of a business at a certain time, and (b) the surpluses or deficits that has accrued over the course of a set period of time.

Accounting is being treated as a business language in which financial performance is reported and evaluated. Knowledge of the same is also beneficial for personal investment and tax planning. Becoming an accountant is not required but it is very useful if everyone understands the accounting and financial concepts and terminology correctly.

1.1 Accounting Streams

Financial accounting, cost accounting, and management accounting are the three types of accounting. We can see the basic difference between the three from the figure given below:



1.2 What are the Fundamental Accounting Concepts?

A number of conceptual issues must be understood in order to develop a solid understanding of how accounting works. These fundamental accounting concepts are listed below.

i. Accruals Concept

When an asset is earned, revenue is recorded, and when it is used, expenses are recorded. According to this idea, a company's income, profits and losses may be

recorded in quantities different from those that would be recorded if those amounts were based on money obtained from consumers or cash paid to vendors and employees. Only financial statements that were created using the accruals principle will have their audits certified.

ii. **The Concept of Conservatism**

Expenses are recorded sooner than revenue whenever there is a reasonable likelihood that they will be incurred. Revenue is recorded only if there is a reasonable probability that it'll be realized. This idea results in financial statements that are more conservative.

iii. **The Concept of Consistency**

When a business chooses to employ a certain accounting technique, it should continue to do so. Financial statements created over a number of periods can therefore be compared with certainty.

iv. **Economic Entity Model**

The business dealings of a corporation and those owners/ founders must be kept apart. This makes sure that a company's financial accounts don't mix up personal and corporate transactions.

v. **Going Concern Concept**

When preparing financial statements, it is necessary to make the judgment that the company will remain in business in the foreseeable future. It is possible for the company to postpone the recognition of revenue and expenses until a later period while they continue to operate under this assumption. In the event that this were not the case, the recognition of all expenses, in particular those pertaining to the present period, would occur earlier.

vi. **Matching Concept**

It is best practice to record expenses that are related to income in the same time that revenue is reported. As a consequence of this, there is no postponement of expense acknowledgment into later reporting periods, and anyone who looks at the financial statements of a company can be certain that all components of a transaction were recognized & recorded at the same time.

vii. **Money Measurement Concept**

Money functions in the economy as both a means of exchange and a unit of value measurement. As a consequence of this, the idea of money measurement dictates that the books of accounts must only contain entries for transactions that can be quantified in terms of money. Transactions that do not involve money are not documented in books since they are not considered to be monetary transactions.

Example 1: A productive meeting with a potential customer is a significant event, but it is not something that can be recorded in the books of accounting.
Example 2: Employees are extremely valuable resources for any company; nevertheless, it is impossible to quantify their worth in monetary terms, so their contributions are not recorded in the books.

Questions to be asked:

1. Business run by an individual is called __________.
2. ___________ is the type of corporation present in India only.
3. Partnership is the type of association among the people who admitted to dividing the gain. (True)
4. An individual who has a legal interest in an institution is called a creditor. (false)
5. The commercial matters are kept free from individual matters with the help of _____________ (entity concept)
6. ______________ make sure that the revenue and cost of the firm run parallel to each other.
7. Matching concept is a financial concept in which costs are identified in the same financial period as profits (true).

2. Bookkeeping

We know from the previous discussion that Financial Accounting involves (a) the recording of data and (b) the strategies used for the presentation of data that are utilized for recording a variety of transactions. This process of recording the data is referred to as "bookkeeping." The data that was captured is then condensed into a summary and organized in a methodical fashion before it is provided to a variety of consumers in the form of financial information/ statements.

"Bookkeeping" is considered to be one of the roles of financial accounting. Bookkeeping comprises the keeping of accurate records and books, as well as the recording of all the relevant details of any and all transactions that occur in the normal course of business. Transactions in a business can be broken down into a number of different primary operations and categories, such as sale, purchase, asset, and so on. For the purpose of recording transactions linked to these operations, separate books are maintained, and the specifics of each transaction are written down in those books.

2.1. Why are books of accounts kept?

Having current knowledge of what is happening in business is crucial. This encourages timely and proper action. In order to identify the sickness, its causes, and its therapies, a doctor needs details regarding the patient's physiological circumstances. Similar to this, in order to decide on the best course of action for the future, the business owner, lender, or creditor must be knowledgeable of the latest financial status of the company. Because it helps to manage and present the latest financial status of the organization, bookkeeping is crucial. The following justifications support the recommendation to keep books of accounts:

- They offer information that is as current as possible regarding the company.
- The results of transactions that were carried out within the time period under examination are reflected in them.
- At predetermined intervals, they report any relevant information regarding the state of the company.
- They provide assistance to governments and other authorities in determining the effect that different taxes have on a certain population.

- They are useful tools for analyzing the performance of businesses and comparing the results of the operations of other companies in the same industry.

2.2. Bookkeeping with Double Entry

For this reason, the Double Entry Bookkeeping System is predicated on the idea that every monetary exchange has countervailing results. There are just two possible outcomes to any given transaction: "debit" or "credit," and both are always equivalent. So, after the fiscal year is over, the total debits and total credits should be the same. You must input the debit entry data with the credit entry for a particular transaction.

2.2.1. Accounts Transactions Using Double Entry System

When conducting business, a promoter will engage in a number of different transactions. The effect that these transactions had on the company's finances is reflected in the books of accounts. Only those transactions that include the transfer of money or the trade of goods or services having a monetary value are subject to the requirements of accounting treatment. There is the potential for the following kinds of transactions:

a) Exchanging goods for cash/credit
b) Service exchange for cash or credit
c) Exchanging assets for cash/credit
d) Paying cash to creditors
e) Receiving cash from debtors
f) Exchanging goods for cash
g) Trade of goods for services

Thus, various types of transactions occur in business, and they serve as the starting point for accounting. Transactions are classified into two types:

(I) Cash Transactions and
(II) Credit Transactions

A cash transaction involves the exchange of money, whereas a credit transaction involves the obligation to pay or receive money in the future.

2.2.2. Types of Accounts:

Transactions entail the use of accounts. An "account" is a need for every transaction. There are a total of three different account types:

i. Personal Account or Individual Account: This category comprises all accounts held by both individuals and organisations, including businesses, corporations, societies, and others.

ii. Assets Account: All asset kinds fall under this heading. All financial investments in tangible or intangible items with utility or use value are considered assets. Additionally, these assets can be sold and turned into cash.

iii. Income & Expenditure Account: All accounts that indicate the business's revenue income, and revenue expenditure are included in this category of accounts.

2.2.3. Debit and Credit Rules

In a bookkeeping system with double entries, each transaction has an impact in two different areas. The first one is known as a "Debit," and the second one is known as a "Credit." As a consequence of this, every transaction will have at least one debit effect and at least one corresponding credit effect. As was indicated before, there are regulations governing the process of debiting and crediting different accounts, and these accounts can be broken down into three primary categories. The Double Entry Bookkeeping System relies on these guidelines as its fundamental building blocks for accounting. The following are the rules that apply:

i. **Personal Accounts Rule:** ***"Debit the Receiver and Credit the Giver."***

Explanation: Any individual who is a party to a transaction has the potential to play either the role of a receiver or a giver of money, assets, or services when there is no immediate consideration involved. The account of the person who receives something is reduced, while the account of the person who contributes something is increased.

ii. **Rule for ‘Assets Accounts’:** ***"Debit what comes in and Credit what goes out."***

Explanation: In the course of business, various goods and assets may come and go. When assets or goods are brought into the company, the corresponding accounts are debited. On the other hand, the corresponding accounts are credited if assets or goods are removed from the company as a consequence of a transaction.

iii. **Rule for 'Income-Expenditure Accounts': *"Debit Expenses and Losses and Credit Incomes and Gains"***

Explanation: All of the income and expense accounts are consolidated into this one group of accounts. The appropriate account receives a credit for the appropriate amount of revenue income generated throughout the course of the business, and the relevant account receives a debit for the appropriate amount of revenue expenses made throughout the course of the business.

2.2.4. Steps for Recognizing a Debit or Credit Effect

i. Determine the extent of the accounting treatment that is required for the transaction.
ii. Determine which of the two accounts is being used for the transaction by looking at both of them.
iii. Apply the debit and credit rules to the accounts that have been identified, taking into account the accounts' respective categories.
iv. It ought to go without saying that "credit entries" and "debit entries" cannot coexist in the same transaction because they refer to opposite sides of the same transaction. A debit entry and a credit entry are essential components of every transaction.

2.3. Books required for a simple accounting system:

A simple financial accounting system is recommended for a small industrial enterprise. Such businesses must keep the books as outlined below. Businesses can quickly obtain an accurate and fair picture of the activities by doing so.

a. Journal: This has an accurate record of all transactions (except those that are to be recorded in subsidiary books).
b. Supplementary books (for journal)

c. Purchase book: The purchase book contains all transactions relating to purchases, whether made with cash or credit. Additionally separately documented in this section are purchase returns.
d. Sales book: The sales book contains a record of all credit or cash sales transactions. Transactions related to sales returns are likewise kept separate.
e. Ledger: All accounts associated with transactions noted in the journal or its subsidiary books are maintained here, and any necessary entries are made.
f. Cash book: The 'cash' account is kept in the cashbook, a subbook of the ledger. Petty cash transactions are also tracked individually in this section.Bank book: A bankbook is a subsidiary book of the ledger where the 'bank' account is kept.
g. Stock register: This is a register that keeps track of stock movement.

2.4. Journal Entries

A journal entry is the first entry in the books of accounts, identifying and note down/ noting the debit and credit impacts of each transfer of funds on accounts, along with a proper description. Journal entries help to prepare several books of accounts. A suggested format for keeping a journal and writing journal entries is as follows:

JournalentriesinthebookofM/s.................				
	Particulars	Ledger Folio No.	Debit (Amount)	Credit (Amount)

Figure 2.1. Format of a Journal

Explanation:

i. Date: journal entries must be written in chronological order. Maintaining daily records of each transaction is recommended. In the "Date" column, include the year, month, and date of the transaction being recorded in the journal.
ii. This column defines the account to be debited as well as the account to be credited for each transaction.

iii. Ledger Folio Number: The third column contains the relevant ledger accounts' folio numbers. This allows you to track and verify each transaction's posting.

iv. Debit and credit: This column displays the debit and credit amounts for each account. The total debits and credits are calculated at the end of each page and carried over to the next page.

2.5. Ledger

A ledger is a book that contains information about all accounts in which transactions are recorded. It records all business transactions transferred from the journal or subsidiary books in a condensed and classified format. The ledger is the main book in the double entry bookkeeping system. It has current details on every account; for instance, if a business owner wants to know how much money they owe Mr. P, they may look up Mr. P's account in the Ledger. The owner would have to review each transaction involving Mr. P to ascertain the payment liability if such accounts weren't recorded in the ledger. This activity takes a lot of time and is inconvenient. It is impractical for organizations with a high volume of transactions to constantly review the main records or journal to ascertain the precise position of any account. Keeping a ledger is essential as a result.

The following is a suggested format for keeping an 'account' in the ledger:

Debit Side Account			(Name of the Account)				Credit Side
Date	Particulars	Folio No.	Amount	Date	Particulars	Folio No.	Amount

Figure 2.2.: Format of a Ledger

Explanation: The format of a ledger account indicates that it has two sides: a debit side (on the left) and a credit side (right-hand side). The four parts on each side—"Date," "Particulars," "Journal Folio Number," and "Amount"—are all required.

i. Date: This column contains the date that a transaction was recorded in the journal book from which it was transferred to the ledger account.

ii. Particulars: This column includes the name of the account where the relevant credit or debit (under the double entry principle) is found.

iii. Journal Folio Number: This column contains the page number of the journal book or subsidiary book from which the transaction was added to the account.

iv. Amount: This column includes the amount that has been debited or credited to the account.

2.6. Transactions:

As transactions take place, they are documented in the journal book or subsidiary books. The ledger is then updated with the appropriate records. Posting is the process of moving entries from the ledger's relevant accounts to the journal or subsidiary books. Amounts written in the journal book's debit column that debit an account are posted to the ledger's debit side. The account's credit side is posted when an account is credited in the journal book. Make that the name of the account where the entry is posted does not appear in the details box when posting entries. Rather, state the name of the other account whose balance is impacted by the transaction. Each entry for an account's credit side should start with the word "By," and each entry for the account's debit side should start with the word "To" (in the "Particulars" column).

2.6. Balancing the Account

The total of the postings to the account's credit side and debit side are typically not equal. The "balance" of the account is the margin by which the sum of any side (debit or credit) exceeds the sum of the other side. The balance is referred to as a "debit balance" if the amount of the debit side is bigger, and a "credit balance" if the opposite is true. For example:

i. Following accounts always have debit balances:

- Asset’s Account
- Debtor’s Account
- Cash Account/Bank Account
- Stocks Account
- Losses Account
- Revenue Expenses Account

ii. Following accounts always have credit balances:

- Creditor’s Account
    - Gain’s or Profit's Account

- Revenue Income's Account
- Interest Received
- Bank Loan Account

2.7. **Purchase book:** The purchase book contains all transactions relating to purchases, whether made with cash or credit. Additionally separately documented in this section are purchase returns.

2.8. Sales Book: The sales book contains a record of all credit or cash sales transactions. Transactions related to sales returns are likewise kept separate.

2.9. Cash Book: A cash account is all that the "Cash Book" actually is. Like all other asset accounts, this one also has to be entered in the ledger. The cash account, often known as the cash book, is kept apart from the general ledger due to the amount of cash transactions and for convenience. This account is subject to the same guidelines that apply to ledger accounts.

2.10. **Bank Book:** The bank account that needs to be recorded in the ledger is known as a bank book, much like a cash book. Due to the rise in bank transactions, it is practical and appropriate to maintain a separate bank account where all bank transactions are posted. This account is therefore maintained separate and is referred to as a bank book. This account is subject to the same posting regulations as other ledger accounts.

2.11. Stock Register: The stock register and stock account are quite similar, as explained. It provides information on the actual closing stock that is on hand at the company so that the owner may physically check it and place more orders.

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3. Financial Statements

Recording all transactions in conformity with generally recognised accounting principles and procedures is bookkeeping's main objective. Simply documenting the transaction, though, is insufficient. Without appropriately classifying the numerous accounts reported for summary, it is difficult to see the business's overall image. Therefore, it is crucial to compile an overview of all the accounting information recorded in different books and to present it in a suitable manner. Accounting information is presented in financial statements to a variety of consumers, including owners, bankers, creditors, tax authorities, governments, suppliers, and others. One can have a meaningful understanding of the financial status of the organisation with the aid of the financial statements.

3.1 Final accounts (Types)

At the end of the fiscal period for which the accounts are written, ledger accounts are typically closed and balances are drawn for generating final accounts. The following statements represent final accounts:

i. Trial Balance
ii. Profit & Loss Statement (P&L)
iii. Balance Sheet

3.1.1. Trial Balance -

The first stage of creating final accounts is a trial balance. To ascertain the ledger entries' arithmetic accuracy is the trial balance's main objective. The fundamental tenet of double-entry bookkeeping is that every transaction has two equal and opposing effects. It indicates that there is a corresponding credit to every debit. As a result, at the end of the accounting period, the sum of all accounts having a "debit balance" and the sum of all accounts with a "credit balance" should be equal. If they are not equal, the accounts will not be accurate

Ledger Folio	Name of Account	Debit closing balance	Credit closing balance
	Total		

Figure 3.1: Format of a Trial Balance

Explanation

i. Ledger Folio: This column contains the folio number (page number) of the ledger or one of its subsidiary books where a particular account is kept. This makes it easier to confirm the veracity of the accounts.

ii. Account Name: This column contains the name of the account whose closing balance is being added to the trial balance.

iii. Debit/Credit closing balance: These columns display the amounts of the debit and credit closing balances of each individual account. It should be noted that a single account cannot simultaneously hold a debit balance and a credit balance. The debit column next to the account name in the trial balance displays the amount of any debit closing balances for each account. Similar to this, the credit column of the trial balance indicates if an account has a credit closing balance.

iv. Total: The totals of the accounts in the debit and credit columns are computed and added after bringing the closing balances of each account from the ledger and its subsidiary books to the trial balance one at a time. It is important to remember:

a. The closing balances of all "Asset Accounts," "Revenue Expense Accounts," and "Losses Accounts" are always debit balances.

b. The closing balances of all "Revenue Income Accounts" and "Gain Accounts" are always credit balances.

c. Accounts of people who owe money to the business always have credit balances, while accounts of people who owe money to the business always have debit balances.

d. "Loan (Taken) Accounts" always have credit balances.

e. There is always a negative balance in the "Cash Account."

If the totals in the trial balance's debit and credit columns do not agree, it indicates that there was an error in preparing the accounting books. The trial balance would be tallied once the error(s) were identified and corrected. However, there are a few errors that trial balance cannot detect, such as:

i. Errors of Principle
ii. Errors of Omission

iii. Errors of Commission
iv. Compensating Errors

3.1.2. Profit & Loss A/C (P&L)

Making a trial balance is a necessary step before accurately making the balance sheet and profit and loss account, the final two crucial financial statements. Its use is still mostly restricted to gauging math accuracy, though. From the financial accounting system, the user is interested in learning the profitability of the business activities over a given time period as well as the status of the company at the end of that time. The statement known as a "Profit and Loss Account" (P & L A/c.) shows how profitable a company's operations were throughout the accounting period.

3.1.2.1 Contents

All of the balances specified in the trial balance are taken, and the accounts for revenue expenditures, revenue type losses, revenue income, and revenue type gains are assigned to P&L A/c. You can then decide whether the company made a profit or a loss at the conclusion of the accounting period using this information. All revenue expenditures and losses are transferred to the debit side of the P&L account, whilst all revenue gains and income is sent to the credit side. If a company's total revenue exceeds its total expenses, it is considered to have made a profit. The corporation is deemed to have lost money if its entire expenses for the accounting period outweigh its total revenues. If the P&L account has a credit balance, it means there was a net profit for the accounting period; if it has a debit balance, there was a net loss. Below is a sample profit and loss statement.

ProfitandLossA/c.of M/S ABC period 2022-23

Debit side **Credit Side**

Particulars	**Amount**	**Particulars**	**Amount**
Net Profit (Balance Figure)		Net Loss (Balance Figure)	
Total:		**Total:**	

Figure 3.2. Format of Profit and Loss Account

Explanation:

i. Particulars: On the debit side, the following accounts are mentioned individually in this column:
   - All revenue expenditure accounts
   - All revenue losses accounts

On the credit side, the following accounts are mentioned:

   - Sales account
   - Stock closing account (if it is adjustment entry)
   - Accounts where adjustment entries have a credit effect

ii. Amount: These figures represent the debit and credit balances of the accounts brought to the P&L account.

3.1.2.2. Keep the following in mind as well:

o All "Income and Expenditure Accounts" are included in the profit and loss statement. Neither person's "Personal Accounts or Asset Accounts" may be brought to the P & L account. The balances of "Personal/Individual Accounts" and "Asset Accounts" are carried over to the following year once all "Income and Expenditure Accounts" have been transferred to the P&L account. All revenue and outlays for the full period are included in the P & L account.

o The sum of the account balances is calculated after moving each account's balance to its corresponding debit and credit side. The company is considered to have made a net profit if the total of the credit side is greater than the total of the debit side. The "Net Profit" made during the accounting period is defined as the difference between the totals on the credit and debit sides of the P&L account. Similar to this, the difference between the totals on the credit and debit sides of the P&L account is known as the "Net Loss" the company experienced for the year. Net profit and net loss data are therefore equal and complementary. The totals on both sides are equal when they are added to the respective debit or credit side. In this instance, total income and total expenses are equal.

Thus,if

i. Total of credit side < Total of debit side = Loss of P&L A/c.
ii. Total of credit side > Total of debit side = Profit of P&L A/c.
iii. Total of credit side = Total of debit side = At PAR of P&L A/c.

The net profit or net loss is the outcome of business operations within the accounting period. They are then moved to the balance sheet, where the promoter's financial involvement is indicated by the capital account, which is increased or decreased in accordance with the net profit or net loss numbers.

3.1.3. Balance Sheet

A balance sheet is a document created to assess the true financial status of a business at a certain point in time (normally the last day of the accounting period). In order to ascertain the results of business activities during the accounting period and (ii) comprehend the financial condition of the firm at a certain moment in time, the balance sheet must be prepared. For the former, one uses the profit and loss account, whereas for the latter, one uses the balance sheet.

All accounts in the "Income and Expenditure Accounts" group are, as was previously stated, assigned to the profit and loss account. The balance sheet is then updated with the accounts from the remaining groups, "Personal or Individual Accounts" and "Assets Accounts." The accounts on the balance sheet are still open. Their closing balances on their balance sheets are carried over to the subsequent accounting period. They are just displayed on the balance sheet to let users know how the accounts are currently doing. In order to make the balance sheet simple to interpret, it should be produced in a precise manner. Below is a suggested format for the balance sheet.

Liabilities	Amount	Assets	Amount
• Capital • Secured loans (Received) • Reserves & Surplus • Current Liabilities Unsecured Loans & Deposits(Received) • Provisions • Profit Accumulated		• Fixed assets • Investments • Loans and Advances (Given) • Current Assets • Stocks------ • Debtors------ • Cash------ • Bank------ • Balance------	

		• Accumulated Losses	
Total		**Total**	

Figure 3.3.: Balance Sheet of M/S ABC as on 31st March-22

Explanation:

The balance sheet, as previously said, shows a company's genuine and fair status at a specific point in time. The balance sheet lists the company's assets and liabilities as a consequence. Assets are defined as the things a company possesses, and liabilities are defined as the things a firm owes. On the balance sheet, liabilities are displayed on the left and assets are listed on the right.

3.1.3.1. Assets

Assets are classified into the following broad categories:

i. Fixed Assets: Since fixed assets are long-term investments, the business's primary goal is to use them to create value. The entire cost of fixed assets at the conclusion of the accounting period is shown on the balance sheet.

ii. Current Assets: In contrast to fixed assets, current assets do not always have the same form. Whatever shape they take, they will almost certainly soon be changed to "Cash" or "Bank Balance."

iii. Investments: The business will occasionally make investments in other enterprises or corporations. The value of these investments is regarded by the corporation as a "Asset."

iv. Loans & Advances (Given): On occasion, the business lends money or gives out advances to other people. Such loans or advances are referred to as assets because of their value. These are not the same as debtors (current assets), where the person is obligated to pay the company after purchasing a product from the company on credit.

v. Fictitious Assets: Fictitious assets are the debit balances of accounts like the Profit and Loss Account, the Accumulated Losses Account, the Expenses Not Written Off Account, and so on.

Let's check our understanding:

1. Cash is a ………………………… (Fixed Asset/Current Asset).

2. The investments made in other enterprises are considered as ………………… (Assets/Liabilities).

3.1.3.2. Liabilities

All "Personal" and "Individual" accounts that the corporation owes are mentioned under liabilities. The following main categories are used to group liabilities:

i. Capital: The promoter's money is a liability in terms of capital. The company owes that sum to the owner.

ii. Reserves and Surplus: The promoter is also entitled to accumulated profit that is not withdrawn and is a component of profit that is set aside for particular uses (s). The company owes that sum to the owner. They are liabilities as a result.

Secured Loans (Received): The total amount of loans that the company has received is a liability. Assets that have been offered as security or collateral to the institutions or people who have issued the loans are used as security for these loans.

Liabilities and assets totals on the balance sheet must add up. If not, there are certain mistakes in the final accounting that need to be found and fixed.

Questions to be asked:

1. The value that we get after deducting personnel, depreciation, and other payments is called tax. (false)
2. ________ is the key book of accounts.
3. The setup involving all the data of the audited account only in the case where cash is credited is called _______ (cash system)
4. Pricing in case of ________________ method rooted in the physical flow of goods.
5. The value of inventory is detected by weighted average price per unit in the case of _______________ method.
6. The tasks that lead to changes in the size and composition of the owner's capital and borrowing of the organization are called

______________.

7. Recording, controlling, estimating, and reporting for cost is part of cost counting (true).

4. Production Management

4.1. The Definition of Production Management:

The application of management principles to the production function in a factory is referred to as production management. In other words, production management entails the planning, organizing, directing, and controlling of the manufacturing process.

At least three developments have resulted in the application of management to the field of production:

I. The first step is the development of a factory production system. There was no such thing as management as we know it prior to the advent of the manufacturing concept. True, people ran businesses of various kinds, but for the most part, these people were business owners who did not consider themselves managers.

II. Essentially stems from the first, namely the growth of large corporations with many owners and the need to hire people to run the business.

III. Derives from the work of many of the pioneers of scientific management who were able to demonstrate the value of some of the techniques they were developing in terms of performance and profit.

It has been observed that the beginning and end points of Production Management in an establishment cannot be defined. The reason for this is that it is interconnected with many other functional areas of business, such as marketing, finance, labour relations policies, and so on. Alternatively, because production management is not separate from marketing, finance, and personnel management, it is difficult to formulate a single appropriate definition of production management.

Production Management is concerned with production-related decision-making. So that the resulting goods and services are produced at the lowest possible cost while adhering to the quantitative specifications and demand schedule. According to this definition, the two main functions of production management are design and control of the production system.

Production management is a set of general principles for manufacturing economies, facility design, job design, schedule design, quality control, inventory control, work study, and cost and budgetary control. This definition explains the main areas of an enterprise where production management principles can be applied. This definition emphasizes that production

management is not a collection of techniques. According to the discussion above, production planning and control are the primary characteristics of production management. In the event of poor planning and control of production activities, the organization may be unable to meet its objectives, resulting in a loss of customer confidence and a slowing of the establishment's progress.

4.2. Production Management Functions:

The discussion mentioned above clearly show that the concept of production management is primarily related to organizations that manufacture goods and services. Previously, these organizations were mostly one-man operations with minor production management issues.

However, as production organizations in the form of factories developed and expanded, more complex problems such as location and layout, inventory control, quality control, routing and scheduling of the production process, and so on arose, necessitating a more detailed analysis and study of the entire phenomenon. As a result, production management was developed in the field of factory management. Initially, the primary function of production management was to control labor costs, which constituted the majority of production costs at the time.

However, as factory systems became more mechanized and automated, indirect labor costs skyrocketed in comparison to direct labor costs, such as product design and packaging, production and inventory control, plant layout and location, transportation of raw materials and finished products, and so on. All of these activities necessitated additional expertise and specialized techniques for planning and control.

In today's world, production management must perform a number of functions, including:

i. Process design and development.
ii. Production planning and control.
iii. Execution of the plan and related activities to achieve the desired outcome.
iv. Administration and coordination of the activities of various components and departments in charge of producing the necessary goods and services.

However, the responsibility for determining output characteristics and an organization's distribution strategy, including pricing and selling policies, is normally outside the scope of Production Management.

4.3. Production Management's Scope:

The scope of production management is indeed broad. Beginning with the selection of a location, production management encompasses activities such as land acquisition, building construction, purchasing and installing machinery, purchasing and storing raw materials, and converting them into saleable products. Other related topics include quality management, maintenance management, production planning and control, method improvement, and work simplification, among others.

In summary, the primary activities of production management are as follows:

I. Input resource specification and procurement, including management, material, and land, labor, equipment, and capital.
II. Product design and development to determine the manufacturing process for converting input factors into goods and services.
III. Monitoring and controlling the transformation process to ensure efficient production of goods and services.

Production Management includes Purchasing, ordering, inventory management, production and dispatch procedures. We will see all these components one by one except production which is a specific process entirely different for all organizations and provides novelty to a business.

5. Purchase Procedures and Methods

The purchase procedure will be determined by the nature, size, standard, location of the establishment & future requirements forecast. The entire purchasing process could be divided into the following steps:

i. Purchase requisition form
ii. Source of supply selection
iii. signing a contract with the supplier
iv. Acceptance of raw materials for food and beverages
v. Commodities are transferred to the ordering department, stores, or cellar.

5.1. Methods of Purchasing

There are various purchasing methods. Generally, due to the location and availability of merchandise, some of the methods used in most food and beverage establishments are described below: -

5.1.1. Purchasing contracts:

A contract is entered into with a supplier for the commodities to be supplied on a regular basis at a reasonable price. A contract is a legal document, and the terms of the contract should be carefully drafted, preferably by the firm's solicitors. ***Contracts are classified into two types***:

i. **Specific period contract**: it is intended to determine the source of supply and the price of goods for a set period of time, such as three or six months. Bread, butter, milk, cream, and so on.
ii. **Quantity Contract:** The goal of a quantity contract is to ensure the continuous supply of a specific quantity of an essential item at an agreed-upon price over a specific trading period. Most suitable for fruits and vegetables, for example.

5.1.2. Purchase clauses: the period, estimated quantities, reservation of the establishment to decide a contract between supplies, purchase specification, removal of rejected food by the supplier, chargeable containers, power to purchase in default, in case of a dispute-an agreed party, indemnity against damage, prevention of corruption, the place of delivery, invoices, payment of invoice, service of notice to break a contract

5.1.3. Periodical purchasing:

The establishment's needs are estimated on a regular basis, and regular orders are placed on a weekly/fortnightly/monthly basis. This method ensures that stocks are kept at a consistent level. On the basis of periodic requirements, a master quotation is prepared. Orders are placed based on the quoted price and available storage space.

5.1.4. Daily market list/daily market quotation/by requirement:

This method is typically used for daily purchases of perishable goods. A list of approved suppliers is being compiled. The executive creates a daily market list based on a quick inventory of the food. Following receipt of the "daily market list," the purchasing office contacts each approved supplier by phone and requests a price quote for each item required. The quoted prices are entered on the daily market list, and the purchase officer decides where to place the order for each item. A proper system for the same may be maintained with appropriate records.

5.1.5. Market purchasing:

In this method, the establishment's needs are estimated. Quotes are requested from various commodity suppliers. The quantity and prices are compared, and orders are placed with the firm with the price and quantity of provisions in mind.

i. **Cash & Carry Market:** The cash and carry method is best suited for small and medium-sized establishments. The buyer has complete freedom to purchase from the market at a competitive price, and he or she can personally check the quantity and taste of the item. But they are required to pay in cash for all items purchased and provide his/her own staff and transportation to collect the items from the point of purchase.
ii. **Cost Plus Method:** The cost-plus method is better suited for welfare catering institutions such as hospitals and boarding houses. The approved supplier is paid the same price he paid for the commodities plus an agreed percentage to cover handling costs, delivery charges, and a profit margin.
iii. **Total supply method**: Some suppliers are able to provide a full supply service for all commodities. Such a supplier may be agreed upon by a food and beverage establishment. This system has the advantage of only requiring one supplier to negotiate with, a lower volume of paperwork, and fewer deliveries. Before placing an

order, a proper purchasing procedure requires obtaining at least two quotations from two dealers for each item.

5.2. Purchase indent:

Non-perishable items are purchased under the authority of a purchase indent, which can originate. If one of the following conditions occurs:

i. A regular storeroom inventory item has reached its pre-determined minimum stock level. The storekeeper/manager would determine the minimum stock level with the assistance of the consuming department head.
ii. A department requires a non-storeroom inventory item, and the indent must come from the department head and be approved by the top authority.

Purchase indents must be made in three copies:

- In the case of standard storeroom items:

i. Department of original purchase
ii. Duplicate for department head and stores
iii. Triplicate to stores

- In the case of non-storeroom inventory:

i. Department of original purchase
ii. Distribute to retailers
iii. Indenting department, three copies

5.3. Purchase order:

This is another important document that must be issued for all ordered items. This should include all items ordered, the delivery time, payment terms, the agreed-upon price, and any other conditions/institutions.

All purchases must be made in accordance with the purchase indent or standard list. Except for standing rate contact items, a purchase order is issued for all items.

5.4. Centralized Purchasing System:

The centralized purchasing system is very popular in chain operations. The requirements of each individual unit are relayed to a central office in this system. The central office determines the total requirements for all units and then makes total purchases for either individual unit delivery by the dealer or centralized delivery. Top management makes the decision to centralize purchasing. The primary benefits of central purchasing are as follows:

i. Volume purchasing results in lower prices.
ii. Possibility of obtaining desired quality due to a wider range of markets
iii. Purchases made in accordance with specifications
iv. Keeping a larger inventory to ensure consistent supply to individual units.
v. Individual food purchasers must be checked and controlled.

5.5. Method of periodic order:

Non perishable goods have a longer shelf life than perishable goods. These items necessitate infrequent ordering and free up the steward to attend to perishables. The person responsible for the job, with the advice of management, establishes ordering periods such as once a week, twice a week, or once a month. He/she, then, goes through the entire inventory of non-perishable items and decides how much of each to order.

5.6. Competitive purchasing-price method:

In this procedure, quotations are requested from one or more purveyors/suppliers, and orders are placed where terms are most advantageous to the buyer, after all price, quality, yield, and service elements have been considered.

i. Ensure that the purchasing agent is purchasing for use rather than stock
ii. Mechanics of purchasing- must provide the necessary information
iii. Daily perishables investment
iv. Market quotations and purchase order sheets are distributed

5.7. Standing orders/purchase orders on file:

Not all perishables must be ordered against a market quotation and purchase order, as items such as milk, ice cream, and so on can be ordered without first obtaining a quotation. Milk

and cream must be ordered daily on a forecast need basis, considering the forecasted number of covers and previous consumption records. However, it is critical that the person reviewing the bills has access to the most recent prices for these items.

5.8. Worksheet for comparing daily purchase prices:

The daily purchase comparison worksheet is posted from the daily invoices, with the unit price and weight of all purchases. The unit price but not the quantity of all other perishable food items will also be posted daily; this information will be used for

i. Costing purposes.
ii. Report on monthly weighted/price competition

6. Inventory Management

The process of ordering, storing, using, and selling a company's inventory is referred to as inventory management. This includes raw material, component, and finished product management, as well as warehousing and processing of such items.

i. Inventory management encompasses the entire inventory management process, from raw materials to finished products.
ii. Inventory management attempts to streamline inventories in order to avoid both gluts and shortages.
iii. Just-in-time (JIT) and materials requirement planning are two major methods for inventory management (MRP).

6.1. Recognizing importance of Inventory Management: Is it an asset or a liability?

One of a company's most valuable assets is its inventory. A company's inputs and finished products are the heart of its business in retail, manufacturing, food services, and other inventory-intensive industries. A lack of inventory when and where it is needed can be disastrous.

At the same time, inventory can be considered a liability (if not in an accounting sense). A large inventory is vulnerable to spoilage, theft, damage, or changes in demand. Inventory must be insured, and if it is not sold in a timely manner, it may be sold at a loss—or simply destroyed.

Inventory management is critical for businesses of all sizes for these reasons. Knowing when to restock inventory, how much to buy or produce, how much to pay, and when to sell and at what price can all become complicated decisions. Small businesses frequently keep manual inventory records and use spreadsheet (Excel) formulas to determine reorder points and quantities. Larger companies will use enterprise resource planning (ERP) software. The largest corporations make extensive use of highly customized software as a service (SaaS) applications.

Depending on the industry, appropriate inventory management strategies differ. An oil depot can store large amounts of inventory for extended periods of time while waiting for

demand to increase. While storing oil is costly and dangerous—a fire in the United Kingdom in 2005 resulted in millions of pounds in damage and fines—there is no risk that the inventory will spoil or go out of style. Sitting on inventory is not an option for businesses dealing in perishable goods or products with extremely time-sensitive demand—for example, 2021 calendars or fast-fashion items—and misjudging the timing or quantities of orders can be costly.

Balancing the risks of inventory gluts and shortages is especially difficult for companies with complex supply chains and manufacturing processes. Firms have developed several inventory management methods, including just-in-time (JIT) and materials requirement planning, to achieve these balances (MRP).

Important*: Because some businesses, such as service-based, do not have physical inventory, they must rely on service process management.

6.2. **Inventory Accounting**

Inventory is a current asset because a company intends to sell its finished goods within a short period of time, typically a year. Before inventory can be recorded on a balance sheet, it must be physically counted or measured. Companies usually keep sophisticated inventory management systems that can track real-time inventory levels.

Inventory is accounted for in one of three ways: first-in-first-out (FIFO), last-in-first-out (LIFO), or weighted average. An inventory account is typically divided into four categories:

i. Raw Material: Raw materials are the various materials that a company purchases for its manufacturing process. Before a company can sell a finished good, these materials must go through extensive processing.
ii. Work in process (also known as goods-in-process): Raw materials that are being transformed into a finished product.
iii. Finished Goods: Finished goods are finished products that are ready for sale to a company's customers.
iv. Merchandise: Finished goods purchased from a supplier for future resale.

6.3. Methods of Inventory Management

Various inventory management methods will be used by a company depending on the type of business or product being analyzed. Just-in-time (JIT) manufacturing, materials requirement planning (MRP), economic order quantity (EOQ), and days sales of inventory are some of these management methods (DSI).

6.3.1. JIT (Just-in-Time Management) — In the 1960s and 1970s, Japan pioneered this manufacturing model. Toyota Motor (TM) made the greatest contribution to its development. By keeping only, the inventory required to produce and sell products, companies can save significant amounts of money and reduce waste. This method saves money on storage and insurance, as well as the cost of liquidating or discarding excess inventory. JIT inventory management can be dangerous. If demand unexpectedly spikes, the manufacturer may be unable to source the inventory required to meet that demand, harming its customer reputation and driving business to competitors. Even minor delays can be problematic; if a key input is not received "just in time," a bottleneck can occur.

6.3.2. Materials Requirement Planning (MRP) — This inventory management method is sales-forecast dependent, which means that manufacturers must have accurate sales records to accurately plan inventory needs and communicate those needs to materials suppliers on time.

6.3.3. Economic Order Quantity (EOQ) — In inventory management, this model calculates the number of units a company should add to its inventory with each batch order in order to reduce total inventory costs while assuming constant consumer demand. In the model, inventory costs include holding and setup costs. The EOQ model aims to ensure that the appropriate amount of inventory is ordered per batch, so that a company does not have to place orders too frequently and does not have an excess of inventory on hand. It is assumed that there is a trade-off between inventory holding costs and inventory setup costs, and that total inventory costs are reduced when both setup and holding costs are reduced.

6.3.4. Days Sales of Inventory (DSI) — is a financial ratio that indicates the average number of days it takes a company to turn its inventory, including work-in-process goods, into sales. DSI is also known as the average age of inventory, days inventory outstanding (DIO), days in inventory (DII), days sales in inventory, or days inventory. The figure represents how many

days a company's current stock of inventory will last, indicating the liquidity of the inventory. A lower DSI is generally preferred because it indicates a shorter time to clear out inventory, though the average DSI varies by industry.

Other methods of inventory analysis exist. If a company frequently changes its inventory accounting method without reasonable justification, it is likely that its management is attempting to paint a more positive picture of its business than is true. The SEC requires public companies to disclose LIFO reserves that can make LIFO inventories comparable to FIFO inventories.

Inventory write-offs on a regular basis can indicate a company's difficulty selling finished goods or inventory obsolescence. This can also raise concerns about a company's ability to remain competitive and manufacture products that appeal to consumers in the future.

7. Cost Control

Cost control is an important aspect of growing a company's finances and increasing its profitability. Understanding cost control methods can help you keep your projects on budget and increase project profitability. In this section, we will define cost control, explain why it is important for businesses, and discuss the various cost control methods.

Cost control is a finance’s professional practice that analyses a company's overall expenses and reduces project costs to increase profit. A company typically hires finance professionals to monitor cost performance, plan budgets for each project, and change projects that can improve a company's financial performance. Finance professionals also develop, maintain, and organize a project's budget from start to finish to ensure that employees adhere to the budget. The goal of cost control methods is to improve a project's financial performance while lowering its costs.

7.1. The significance of cost control:

Cost control enables businesses to stick to a strict budget, which keeps their finances stable and can help their projects become more profitable. Here are some of the reasons why businesses must employ cost-cutting measures:

- Budgets aid in project management: Cost control methods frequently involve establishing a strict budget for a team to adhere to, which aids in project management. Employees may feel more compelled to complete a project by the budget's deadline if the budget calls for it to be completed by a certain time.
- Keeps project costs from rapidly increasing: Using cost control methods can help keep project costs from rapidly increasing as the project progresses. If project members believe the budget does not cover all of the project's costs, they can consult a financial professional.
- Maintains profitability: Cost control methods allow the revenue generated by projects to be greater than the cost of the project, thereby maintaining profitability and increasing a company's finances.

7.2. Cost-cutting factors:

Several factors are involved in project cost control monitoring, including:

7.2.1. Labor costs:

The cost of labor is the total wages paid to employees working on a project, including employee benefits and taxes. When budgeting a project, it is critical to include the cost of labor because a project may involve multiple employees working at the same time. For example, when creating a budget, make sure to include the total number of employees on the project as well as the length of time each employee can work on the project to get an accurate estimate of the total cost of the project.

7.2.2. Material costs:

The cost of materials is the total cost of all supplies and equipment needed for a project. This includes materials ordered before the project begins, during the project's completion, and after the project is completed.

7.2.3. The Actual (true) cost:

The total expenses incurred by a project from start to finish are referred to as the actual cost. This includes the cost of labor, materials, and any other project-related expenses. When we look at them in totality, we understand the need and point to control cost before the start of the work or during mid-course revision.

7.2.4. ROI (Return on Investment) (ROI):

Return on investment (ROI) measures how profitable a project is in relation to the amount of money invested in it. Having a high ROI means that the project brought in more money than it cost. Before starting the work, an anticipated RoI is going to give a clear picture of the returns and a need for cost control if any.

7.3. Five Cost-Cutting Strategies

Here are five cost-cutting strategies that can help a company maintain and track its overall costs:

7.3.1. Proper Budget Planning:

Budget management is one method of cost control that most businesses use when starting a new project. Setting aside enough time to create an accurate

budget for new projects is critical because budgeting helps estimate costs, organize finances, and ensure cost variance is kept to a minimum. When budgeting, businesses consider all aspects of the project, such as how many employees are required for the project, how long it may take to complete, and how much material is required.

It is critical to leave enough room in your budget for any unexpected costs. For example, some projects may end up taking longer than expected or requiring more material than anticipated, which is why it's critical to budget for unexpected changes.

7.3.2. Using checkpoints, track all expenses.

Monitoring all project expenses is a common cost control method used by businesses to ensure that the budget is followed correctly. Businesses frequently have checkpoints that are analyzed on a regular basis throughout a project to ensure that team members are staying within budget and to determine if any changes need to be made, such as if team members request more time or material to complete the project. These checkpoints can be analyzed by professionals on a weekly to monthly basis.

Using these checkpoints, finance professionals can analyze the changes that are required and adjust the budget accordingly. Using this cost-cutting method allows for changes that have a minor impact on the budget.

7.3. 3.Using change management systems

Change control systems are cost-cutting methods that consider any changes that may have a significant impact on the budget. These changes can result from any issues that arise during the project or from significant delays that cause the project to miss the deadline, resulting in an increase in labor and material costs. Change control systems monitor all changes made to the project to ensure that professionals make budget adjustments. They also document changes and ensure that all changes are necessary for the project.

7.3.4. Effective time management

Time management is a cost-cutting strategy that involves meeting project deadlines in order to keep project costs low. When a project is delayed, the

cost of the overall project's expenses rises because they continue to use materials and employees to complete the project, lowering the project's profitability.

7.3.5. Keeping track of the earned value

Earned value is a popular cost-cutting strategy among accountants. It entails multiplying the percentage of project work completed by the budget at the time of project completion. Earned value assists professionals in predicting the financial outcome of a project based on the project's completion time, total expense, and overall cost.

8. BUDGETING

A budget is an estimated statement. It is prepared by both businesses and the government. It is done to achieve a specific goal. A budget is a financial and/or quantitative statement prepared and approved prior to a specified period of time of the policy to be pursued during that period in order to achieve a specific goal. It may include income, expenditure, and capital employment. It is frequently used for control purposes.

8.1. Budgetary Management

It is a process in which a budget is established and actual results are compared to the budget to determine variances. It entails the creation of budgets that link executives' responsibilities to the requirements of policy, as well as the continuous comparison of actual and budgeted results in order to secure the policy's goal through individual action or to provide a foundation for its revision.

- **Planning:** A set of targets/goals is frequently required to guide and focus individual and group actions. Planning not only motivates employees but also improves decision-making overall.
- **Directing**: Business is extremely complex, necessitating more formal direction and coordination. Once the budgets are established, they can be used to direct and coordinate operations in order to meet the stated objectives.
- **Controlling:** Actual performance can be compared to planned goals. This provides immediate feedback on performance. Budgeting also helps to prevent unplanned ad hoc spending.

8.2. Benefits of a Budgetary Control System

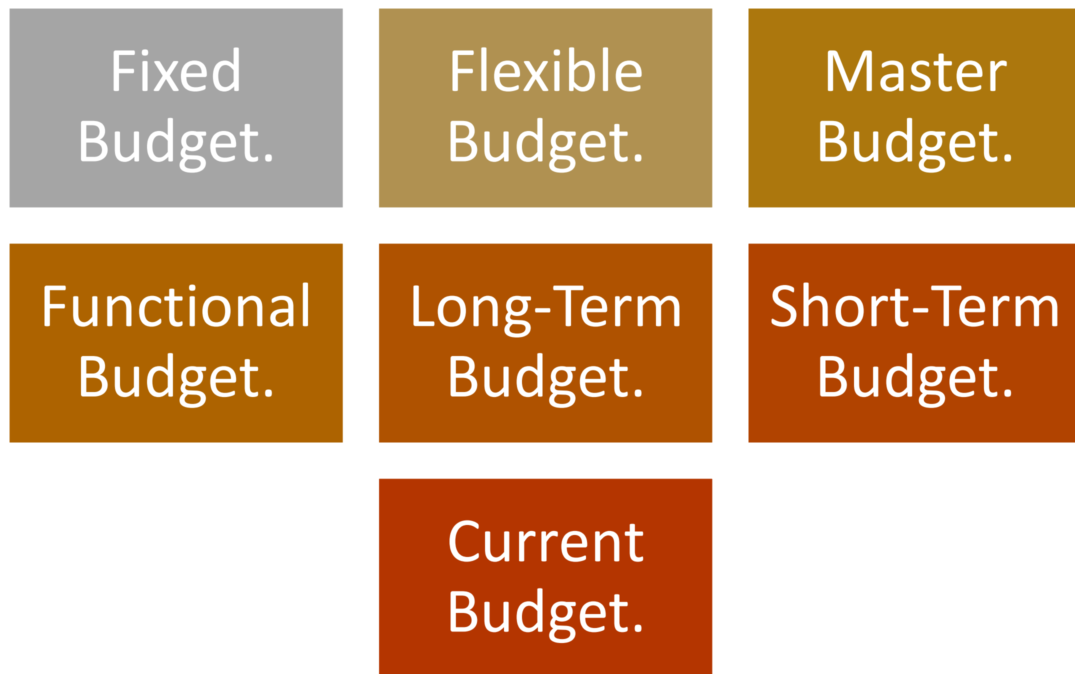
- Allows managers and administrators to carry out their duties more efficiently.
- Provides a yardstick for measuring and evaluating individual and department performance.
- By comparing actuals to the budget, it reveals deviations from the budget; this aids in the expedited review process.

- Creates a favorable environment for the implementation of a standard costing system.
- Serves as a systematic foundation for developing future policies and objectives.
- Instills a sense of cost consciousness and goal orientation.
- As activities are planned and executed effectively, various resources are effectively utilized.

8.3. Budgetary Control System Components

- **Master Budget:** The master budget represents a company's policy for a given time period, with details provided in a series of individual budgets known as functional budgets. Physical, cost and profit budgets are the three broad categories of functional budgets.
- **Budgets for Physical Assets:** Physical budgets are those that contain information in physical units about sales, production, and so on, such as the number of sales, quantity of production, inventories, and manpower budgets.
- **Budgets for costs:** Cost budgets are those that provide cost information for manufacturing, selling, and administration, for example, manufacturing cost, selling cost, administration cost, and research and development cost budgets.
- **Profit margins:** Budgets that allow for the calculation of profit, such as sales budgets, profit and loss budgets, and so on.

8.4. Budget Types



8.4.1. Fixed Budget

A fixed budget is one that is intended to remain constant regardless of the level of activity attained. This budget is appropriate for Fixed Expenses. It is also referred to as a static budget.

Because of its rigidity, a fixed budget is unsuitable in a dynamic environment or over a long period of time. It is not appropriate in situations where labour costs, material costs, and other factors are constantly changing.

8.4.2. Flexible Budget

The flexible budget displays the expected results of the responsibility center for various activity levels. A flexible budget is a collection of static budgets for various levels of activity. When creating a flexible budget, revenues and expenses are classified as Fixed, Variable, and Semi-variable.

Most of the time, the level of activity varies from period to period due to changes in demand, seasonality, or changing circumstances. A flexible budget is appropriate in such industries/government organizations.

8.4.3. Functional Budget

Functional budgets are budgets that are related to a specific function or task within an organization. Purchase budget, sales budget, production budget, plant utilization budget, and cash budget are some examples.

8.4.4. Master Budget

It is a synthesis of the various functional budgets. It is based on the objectives that have been established. It serves as the foundation for budgeted P&L A/c and forecasted Balance Sheet.

8.4.5. Budget for the Long-Term

Long-term budgets are those that are prepared for periods longer than a year. Budgets of this type are useful for business forecasting and strategic planning. Budgets for capital expenditures and research and development, for example.

8.4.6. Budget for the Short-Term

Short-term budgets are those that are prepared for periods of less than a year. For example, Cash Budget. Such budgets are prepared on a regular basis for comparison and action in order to keep variation under control.

8.4.7. Budget for the Present

A current budget is one that is established for use over a short period of time and is related to current conditions.

8.4.8. Budgeting with No Base (ZBB)

It refers to creating a budget from scratch. ZBB is a budgeting method that requires each cost element to be specifically justified as if the budgeted activities were being undertaken for the first time.

Each activity must be justified in terms of continued usefulness in order to receive funding during the budgeting process. Almost every activity's budget is initially set to zero under ZBB.

8.4.8.1. Advantages

- Provides a systematic approach for evaluating various activities and ranking them in order of preference for scare resource allocation.
- Ensures that every activity/function performed is critical to the achievement of goals. Allows for the allocation of resources for various activities/functions only after a thorough cost-benefit analysis.
- Wasteful spending is simple to identify and eliminate.

Questions to be asked:

1. Cost accounting help in the identification of activities that lead to a profit of any type (false).
2. The costs which get influenced by the action of a specific member of an undertaking is the controllable cost (true).
3. All the indirect factory costs are usually merged into an individual cost pool known as ________________ or ______________.
4. Cost which is important to complete the product is only included in the product cost for the manufacturing institution. (true)
5. The relationship between overhead costs and activities for the better allotment of overhead cost is established by ___________.
6. The cost that changes with the volume of activity is known as semi _ variable cost (false)
7. The method of budgeting that requires a cost element to be particularly justified, as the activities to which the budget is related was being undertaken for the first time, is called ________.

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