

FIXED
&
FLEXIBLE
BUDGET

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On the basis of Flexibility-

- ✓ On the basis of flexibility the budget may be classified into two categories namely-
- ✓ Fixed or Static Budget, and
- ✓ Flexible Budget

Fixed or Static Budget-

- ✓ **Definition-** According to ICWA, London- “Fixed Budget is a budget which is designed to remain unchanged irrespective of the level of activity actually attained”.
- ✓ The budget in which the objectives and targets are fixed is known as fixed or static budget.

- ✓ Prepared when?
- ✓ It is prepared after a long discussion before the beginning of the year.

- ✓ In fixed budget preparation the essential conditions are-
- ✓ Business nature is not seasonal
- ✓ No effect of external factors on business conditions.
- ✓ Product demand is certain and fixed
- ✓ Regular issue of supply orders
- ✓ Regular supply of inputs
- ✓ Price stability trend is there

Characteristics of a Fixed Budget-

- ✓ Targets achievement is a must, as instructions issued by the management authorities.
- ✓ Fixed aim/objectives/targets of the business firm/unit.
- ✓ It is prepared in normal conditions of business.
- ✓ It assumes that other factors will remain constant in future.

Fixed Budget: Merits/ Advantages/Benefits-

- ✓ **i.** Time saving
- ✓ **ii.** Easy to prepare
- ✓ **iii.** Easy to control
- ✓ **iv.** Easy to forecast about production and sales
- ✓ more accurately

Fixed Budget:

Demerits/Disadvantage/Losses-

- ✓ Based on wrong assumption of other things remaining the same
- ✓ Change is not possible
- ✓ In accurate estimates and data
- ✓ Other factors have great impacts on sales & production activity.

Flexible Budget-

- ✓ **Definition- ICWA London**, “Flexible budget is a budget which, by recognizing the difference between fixed, semi-variable, and variable costs, is designed to change in relation to the level of activity attained”.
- ✓ Flexible budget is the budget in which adjustment is possible according to change in business conditions.
- ✓ Flexible budget is prepared for various capacity/activity levels of production i.e. from minimum to maximum level like- 10%, 20%, 30%, 40%, 100%

Flexible Budget Characteristics-

- ✓ A Flexible budget consists of a series of budgets prepared in respect of different levels of activity during a budget period.
- ✓ It can be changed and adjusted as per the changes in the business conditions.
- ✓ Prepared in advance
- ✓ Prepared for various levels of activity
- ✓ Its nature is dynamic
- ✓ Concerned with a particular period of time
- ✓ Production possible at all levels of productions.
- ✓ Easy to control unfavorable effects of the changes.

Utility of Flexible Budget for the types business and industry.:-

- ✓ Seasonal nature business
- ✓ Business of dynamic nature
- ✓ Business concern operating on international or multinational level.
- ✓ A business in which demand of product is not regular and fixed.
- ✓ A business unit in which lot changes takes places frequently.
- ✓ A business effected by changing government policy.

A business unit or firm in which-

- ✓ Consumers income is changing
- ✓ Consumer habits are changing
- ✓ Consumer interests are changing

Flexible Budget: Advantages/Importance/Merits/Benefits

- Easy to calculate sales, cost, profits at various levels of production capacity.
- Helps in comparison of actual figure with the budget figures.
- Help in cost control by finding the variances in actual figures and budget figures. Steps may be taken to minimum the variance.
- In flexible budget, adjustment is very simple according to change in business conditions.
- It is very easy to know the effects of cost factors on business profits.
- It helps in determination of production level.
- It is prepared to free from the disadvantages of fixed budget.
- Know the impact of external environmental factors on the activities of business.

Nature and Behavior of Cost-

For the preparation of Flexible Budget costs may be divided into three categories-

I Fixed Costs-

- ✓ There are the costs that remain constant at all levels of production.
- ✓ They do not increase with changes in the volume of production.
- ✓ Cost that does not vary but remains constant within a given period of time and a given range of activity in spite of fluctuations in production is known as fixed cost.
- ✓ Examples-
- ✓ Rent or rates
- ✓ Insurance charges
- ✓ Management salary

Variable Costs-

- ✓ There costs tend to vary with the volume of output. Any increase in the volume of production results in an increase in variable cost and vice versa.
- ✓ Cost that varies directly in proportion with every increase or decrease in the volume of output or production is known as variable cost.

Example-

- ✓ Wages of labours
- ✓ cost of direct material
- ✓ Direct material
- ✓ Direct labour
- ✓ Direct expenses

Semi variable Cost-

- ✓ These costs are partly fixed and partly variable in relation to output.
- ✓ The cost that does not vary proportionately but simultaneously does not remain stationary at all times is known as semi-variable costs.
- ✓ It can also be named as semi-fixed cost.

Examples-

- ✓ Telephone Bill
- ✓ Electricity Bill
- ✓ Depreciation
- ✓ Repairs

Methods of preparing Flexible Budget-

- ✓ Multi Activity Method
- ✓ Formula Method
- ✓ Graphic Method

Names of budgets prepared by there authorities

Purchase Manager

- ✓ Purchase Budget
- ✓ Material Budget
- ✓ Stock Budget

Sales Manager-

- ✓ Selling and distribution budget
- ✓ Advertising budget

Production Manager-

- ✓ Production Budget
- ✓ Production cost budget
- ✓ Material budget
- ✓ labor budget
- ✓ production overheads budget
- ✓ Repairs budget
- ✓ Wastage budget
- ✓ Quality budget
- ✓ Plant utilization budget

Finance Manager-

- ✓ Expenditure budget
- ✓ Revenue budget
- ✓ Return budget
- ✓ Administration overhead budgets

Marketing Manager-

- ✓ Advertisement budget
- ✓ Brand budget

Accountant-

- ✓ Master budget
- ✓ Cash budget
- ✓ Capital expenditure budget

Costing Department-

- ✓ Material budget
- ✓ Labor budget
- ✓ Production overhead budget