COST ACCOUNTING
MASTER BUDGET ASSIGNMENT
SUMMER, 2004

The Klein Electronic Company distributes a wide range of electronic components to various manufacturers. The company has a budget horizon of three months and is now putting together a set of budgets for the first quarter of fiscal 2005, which begins July 1, 2004. Klein's balance sheet at June 30, 2004 follows:

ASSETS

Current Assets: Cash		**$60,000**	
Accounts Receivable	**$ 220,000**		
Less Allowance for doubtful Accounts	**(20,000)**	**200,000**	
Inventories		**100,000**	
Total Current Assets			**$360,000**
Property, Plant and Equipment			
Land		**$830,000**	
Building	**$500,000**		
Less Accumulated Depreciation	**(230,000)**	**270,000**	
Equipment	**200,000**		
Less Accumulated Depreciation	**40,000**	**160,000**	
Total Property Plant and Equipment			**1,260,000**
TOTAL ASSETS			**$1,620,000**
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LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities:		
Accounts Payable	**$ 35,000**	
Income taxes payable	**50,000**	
Notes Payable	**60,000**	
Commissions Payable	**60,000**	
Bond Interest Payable	**20,000**	
Bonds Payable, Maturing 7/31/04	**800,000**	
TOTAL LIABILITIES		**$1,025,000**
Stockholders' equity		
Common Stock, $10 par value	**$300,000**	
Retained Earnings	**295,000**	
Total Stockholders' equity		**595,000**
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY		**$1,620,000**
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As the first step in the budgeting process, the sales manager has budgeted sales for the first four months of fiscal 2005 as follows:

MONTH	BUDGETED SALES
July	$450,000
August	525,000
September	800,000
October	820,000

Normally, 90% of sales are on credit and 10% are for cash (customers pick up merchandise and provide their own trucks, paying cash on pick up). The company estimates that credit terms of net 30 result in 30% of credit sales being collected in the month of sale, 60% in the month following and 8% in the second month following, with 2 % uncollectible. Of the balance in accounts receivable at 6/30/04, the credit manager estimates that 80% will be collected in July and 10% in August, with the rest being written off at the end of the first quarter. All uncollectible accounts will be accounted for in a manner acceptable for Generally Accepted Accounting Principles.

The gross profit rate has averaged 45% in recent years. Normally, 70% of a month's purchases are paid for in the month of purchase with the remainder in the following month. The accounts payable balance at December 31 represents December purchases not paid for that month. The company's policy is to maintain an inventory at the end of each month equal to 40% of the following month's budgeted cost of sales.

Commissions equal to 8% of sales are paid in the month following a sale. Fixed selling, general and administrative expenses are $200,000 per month and are paid in the month incurred. The building is currently being depreciated at a rate of $25,000 per year and the equipment $20,000. Depreciation expense is included in the selling and administrative expense budget of $200,000 per month. The company plans to declare a cash dividend of $0.50 per share on September 15, 2004, payable to stockholders of record on September 30, 2004. The payment date will be October 15, 2004.

The bond issue maturing on July 31, 2004 will be replaced by a new bond issue in the amount of $1,000,000. The bond maturing at July 31, 2004 was originally issued at par. However, due to credit ratings and current interest rates, the treasurer expects that the new bond will be issued at 98. The bond will be a 20 year bond, paying interest semiannually and will have a face rate of interest of 8%. The old bond had a face rate of 6%. The company uses the straight-line method to amortize bond premium or discount.

The company plans to purchase $800,000 of new equipment for its Warehouses. It is expected that the equipment will be purchased at the beginning of August, 2004. The new equipment will be depreciated straight line with an estimated useful life of 10 years. The depreciation of new equipment is not included in the above mentioned budget numbers. The company uses the half-year convention for depreciating new assets.

The company will budget a minimum cash balance of $40,000 at the end of each month. Any shortages will require short term borrowing at interest rates of 6%. Any excess should be budgeted first to pay off any existing short term notes payable, which carry an interest rate of 6% per annum; the remainder will be invested in certificates of deposit, having maturities of 90 days, with interest at 2% accruing until maturity. Interest on notes payable will be paid in cash at the end of each month. All transactions involving bonds, purchase of securities, payment on debt are assumed to take place at the **end** of the month. There was no accrued interest related to notes payable at June 30, 2004.
When calculating interest, use a 30 day month, 360 day year. **All calculations should be rounded to the nearest dollar.** The company will accrue any estimated taxes at an estimated tax rate of 35% for the quarter ended September 30, 2004. The taxes payable at June 30, 2004 will be paid in August, 2004. For budgeting purposes, ignore any tax losses that may result from your budgeting assumptions. That is, if the company has a net loss, assume that income taxes will be zero for that period.

PART I
Prepare the following schedules, by month and in total, for the quarter ended September 30, 2004. All schedules should be prepared in a professional manner, with appropriate format and proper headings. Any computations needed should be presented in separate schedules and referred to in your budget schedules.

a. Sales
b. Cash Collections
c. Budgeted purchases of inventory
d. Cash payments for inventory
e. Cash budget, by month and for the quarter.
f. Budgeted multiple step income statement for the quarter ended September 30, 2004(monthly income statements are not required).
g. Budgeted classified balance sheet at September 30, 2004 (Monthly balance sheets are not required).
h. Budgeted statement of cash flows for the quarter ended September 30, 2004. (Monthly statements are not required)

PART II

The President of the Company, Ms. Sevigny, comes to you as you are completing your master budget schedules. She has been calculating several strategic moves and would like your assistance and professional analysis of the implications of these moves. Because she is very busy, she would like only your written analysis, professional opinion and the relevant schedules for each scenario, not a complete master budget for each. However, she would like to see a balance sheet, income statement and cash flow statement for each. Be sure to discuss your recommendations in a brief analysis of each scenario and provide and justify your recommendation to Ms. Sevigny.

SCENARIO I: Ms Sevigny is concerned with cash flows, due to the low sales projections for July, the slowest month of the year.
She has just attended a seminar on Activity Based Management and is intrigued by Just-in-Time inventory techniques. She has heard that such techniques can reduce a company's inventory holding and storage costs and result in improved profitability. She believes that reducing the month end inventories to 20% of the following month's cost of sales will result in budgeting savings of operating expenses $20,000 per month. She would like to see the impact of this change on the company's budgeted profits, current ratio, debt-to-equity ratio and breakeven point.

SCENARIO II: Ms. Sevigny would like input from you. She would like you to suggest a scenario that would improve the company's results. Provide a suggestion (s) and indicate the impact that your suggestion (s) would have on the ratios mentioned in scenario I. Ms. Sevigny is interest in something that she has not already thought of, such as scenario I with different numbers. As in scenario I, attach the *relevant* budget schedules, including the income statement, balance sheet and cash flow statement.

Each student is to design and prepare his/her own spreadsheet. Obviously identical spreadsheets or those bearing too strong a resemblance to one another will result in a 20 point penalty in your grade. Your potential employer is interested in your ability to design a spreadsheet, not your best friend's.