

Budgeting and Controlling – Part 2

The Components of a Complete Budget of an Enterprise

The first article of the series Budgeting and Controlling (BTV-Aktuell 3/1999) has dealt with the new legal regulations obliging corporations to compile a budget. The second part covers the components of a complete budget of an enterprise in more detail.

A complete budget of an enterprise should present the future development in terms of assets, financial state and earnings situation. The development of the assets of an enterprise is shown in the budgeted balance sheet, the development of the financial state in the framework of a finance plan and the development of the earnings situation in a profit plan.

Profit plan, finance plan and budgeted balance sheet, if they are compiled together and all relations and connections between the individual plans have been taken into consideration, are also called Integrated Profit and Finance Planning. One component alone cannot exist in this Integrated Profit and Finance Planning, each is influenced by the two others.

Compilation of the profit plan is the first step in the framework of Integrated Profit and Finance Planning. Based on sales and

variable and fixed costs, the planned result (profit or loss) of the enterprise is determined.

Building on the result of the profit plan, the finance plan is determined. In the framework of the finance plan, liquidity or solvency is planned which means expected liquidity surplus or liquidity deficit resp. The finance plan starts with the planned profit or loss of the profit plan and results in planned liquidity surplus or liquidity deficit for the enterprise for the planned year.

For compiling the finance plan an appraised profit plan must be available. The result of the finance plan can, however, have an impact on the profit plan, namely by liquidity surplus or liquidity deficit. Deficits must be financed, a surplus can be assessed or used for repaying loans. This may, however, have an impact on the profit plan in form of a change in the amount of interest paid or income from interest. With these changed expense or income items the planned result of the profit plan (profit or loss) also varies. Thus, the basis for the finance plan is different and the finance plan must be revised.

This is what is meant with Integrated Profit and

Finance Planning: the result of the profit plan has an impact on the finance plan and the result of the finance plan influences the profit plan. In this way, an exact solution can only be compiled by several successive compilations of profit plan and finance plan. Thus, profit plan, finance plan and also budgeted balance sheet must be compiled in several steps.

The third step in Integrated Profit and Finance Planning is the compilation of the budgeted balance sheet. Basing on the opening balance sheet at the beginning of the business year and under consideration of all changes from the finance plan that effect liquidity, the budgeted balance sheet is compiled for the end of the planned year. The budgeted balance sheet represents the absolute values in the balance sheet at the end of the planned year, the finance plan represents the changes in liquidity or solvency. Thus, the finished or at least preliminary opening balance sheet, as well as an already compiled finance plan, form the basis for a budgeted balance sheet. It happens frequently that finance plan and budgeted balance sheet are compiled simultaneously; every change in the finance plan immedi-

ately changes an item from the opening balance sheet to the budgeted balance sheet.

The calculations described above lead to a complete budget of an enterprise consisting of profit plan, finance plan and budgeted balance sheet. To gain more information of the development of an enterprise within the year, the three components profit plan, finance plan and budgeted balance sheet must be compiled quarterly or monthly. Only in this way, the current development of the enterprise concerning assets, financial state and earnings situation can be planned and assessed correctly.

The next articles of the series Budgeting and Controlling will deal with the detailed structure of profit plan, finance plan and budgeted balance sheet.

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