Cadence forecasted sales revenues based on his projections for both the market growth for the initial software and successful completion of new products. Cross used this data to construct the master budget for the company, which he then broke down into departmental budgets. Cadence and Cross met a number of times over a three-week period to hammer out the details of the budgets.

When Cadence and Cross were satisfied with their work, the various departmental budgets were distributed to the department managers with a cover letter explaining ATC's new budgeting system. The letter requested everyone's assistance in working together to achieve the budget objectives.

Several of the department managers were displeased with how the budgeting process was undertaken. In discussing the situation among themselves, they felt that some of the budget projections were overly optimistic and not realistically attainable.

Required:

1. How does the budgeting process Cadence and Cross used at ATC differ from recommended practice?
2. What are the behavioral implications of the way Cadence and Cross went about preparing the master budget?

(CMA, adapted)

PROBLEM 9–26 Completing a Master Budget [LO 9–2, LO 9–4, LO 9–7, LO 9–8, LO 9–9, LO 9–10]

The following data relate to the operations of Picanuy Corporation, a wholesale distributor of consumer goods:

Current assets as of December 31:	
Cash	$6,000
Accounts receivable	$36,000
Inventory	$9,800
Buildings and equipment, net	$110,885
Accounts payable	$32,550
Capital stock	$100,000
Retained earnings	$30,135

a. The gross margin is 30% of sales. (In other words, cost of goods sold is 70% of sales.)

b. Actual and budgeted sales data are as follows:

December (actual)	$60,000
January	$70,000
February	$80,000
March	$85,000
April	$55,000

c. Sales are 40% for cash and 60% on credit. Credit sales are collected in the month following sale. The accounts receivable at December 31 are the result of December credit sales.

d. Each month's ending inventory should equal 20% of the following month's budgeted cost of goods sold.

e. One-quarter of a month's inventory purchases is paid for in the month of purchase; the other three-quarters is paid for in the following month. The accounts payable at December 31 are the result of December purchases of inventory.

f. Monthly expenses are as follows: commissions, $12,000; rent, $1,800; other expenses (excluding depreciation), 8% of sales. Assume that these expenses are paid monthly. Depreciation is $2,400 for the quarter and includes depreciation on new assets acquired during the quarter.

g. Equipment will be acquired for cash: $3,000 in January and $8,000 in February.