ACC-FPX5610 Assessment 2

Budget Planning Framework

Participative Master-Budget Design for Meridian Medical Devices

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Executive Summary

Meridian Medical Devices needs a budget process that connects strategy, operating assumptions, resource decisions, cash requirements, accountability, and corrective action. This report proposes a participative budget planning framework for the company's portable cardiac-monitor product line. The framework begins with approved strategic goals and a controlled assumptions register. It then converts expected demand into sales, production, direct-material, direct-labor, overhead, cash, and capital schedules before management approves a complete master budget.

The opening quarterly plan assumes sales and production of 10,000 units at $125 per unit. Standard variable manufacturing cost is $83 per unit, fixed manufacturing overhead is $300,000, and budgeted operating income is $120,000. The contribution margin is $42 per unit, the break-even point is about 7,143 units, and the margin of safety is approximately 28.6 percent. A 10 percent volume decline would reduce operating income to $78,000, while a 10 percent increase would raise it to $162,000. The sensitivity shows why Meridian must combine a realistic sales forecast with flexible-budget control.

The recommendation is to use a rolling 12-month forecast, monthly operating reviews, quarterly re-forecasting, and formal variance thresholds. Finance should compare actual cost with a flexible budget at actual activity rather than relying only on the static plan. Budget owners should explain causes and corrective actions, while quality, safety, compliance, and suspected-fraud exceptions are escalated regardless of dollar size. COSO-aligned controls, role-based system access, version control, documented approval, and the IMA ethical standards should protect the integrity of the process.

Purpose and Decision Context

A budget is both a planning instrument and a management-control system. It communicates what the organization intends to accomplish, identifies the resources needed, and creates a basis for comparing actual performance with expectations. OpenStax describes budgeting as a formal way to communicate plans to internal stakeholders and explains that the operating and financial budgets are combined in the master budget (Franklin et al., 2019). The process should therefore begin with strategy rather than with a request for departments to repeat the prior year's spending.

Meridian manufactures portable cardiac monitors in a regulated, quality-sensitive environment. A narrow cost-cutting budget could encourage decisions that reduce testing, delay maintenance, or create unreasonable production targets. The proposed framework balances profitability with product quality, customer service, liquidity, employee capacity, and ethical reporting. It also creates the baseline standards that can later be evaluated through variance analysis.

Budget Planning Framework

Stage	Management Activity	Required Output
1. Strategic direction	Board and executive team define growth, margin, quality, liquidity, and risk objectives.	Approved strategic targets and risk limits
2. Assumptions register	Owners document volume, price, cost, labor, capacity, collection, and financing assumptions.	Version-controlled assumption file
3. Operating budgets	Sales drives production, materials, labor, overhead, inventory, and selling costs.	Linked operating schedules
4. Financial budgets	Treasury and finance convert the operating plan into cash, capital, financing, and budgeted statements.	Cash plan and projected statements

Stage	Management Activity	Required Output
5. Challenge and approval	Finance tests consistency, sensitivities, capacity, and cash feasibility before executive approval.	Approved master budget
6. Execution and monitoring	Managers receive monthly actual-versus-flexible reports with operational measures.	Variance report and action log
7. Forecast and learning	The organization updates the next 12 months using current evidence without rewriting past targets.	Rolling forecast and lessons learned

Note. The approved budget remains the accountability baseline. A rolling forecast updates expectations but does not erase prior performance.

Design principle
Every material budget number should have an identifiable owner, a documented source, a calculation method, an approval date, and a reasonable sensitivity range. A number without this evidence is an unsupported estimate rather than a controlled planning assumption.

Governance and Responsibility

Role	Primary Budget Responsibility	Accountability Focus
Board / audit committee	Approve risk appetite, major capital commitments, financing limits, and final budget.	Independent challenge and oversight
Chief executive officer	Set strategic priorities and resolve conflicts among functions.	Enterprise accountability
Chief financial officer	Own the framework, approve assumptions, and certify affordability and financing.	Budget integrity and liquidity
Controller / FP&A	Maintain models, validate data, prepare scenarios, and issue variance reports.	Reliable analysis and version control
Sales and marketing	Prepare volume, price, product-mix, and customer-collection assumptions.	Revenue forecast
Operations and quality	Plan production, capacity, yields, maintenance, and quality safeguards.	Feasible production plan
Procurement and HR	Support material-price, supplier, staffing, wage, and training assumptions.	Resource and cost standards
Treasury	Prepare cash, debt, covenant, and financing schedules.	Liquidity plan
Internal audit	Test design and operation of key controls without owning the budget.	Independent assurance

The process should be participative but not uncontrolled. Operational managers possess the best information about customers, labor, equipment, and suppliers, while finance is responsible for challenging optimism, inconsistency, unsupported cost reductions, and hidden slack. The IIA Three Lines Model supports this separation: management owns performance and controls, oversight functions monitor and challenge, and internal audit provides independent assurance (Institute of Internal Auditors, 2020).

Baseline Planning Assumptions

Assumption	Budget Basis	Evidence	Owner
Sales and production volume	10,000 units per quarter	Sales pipeline, capacity plan, market forecast	Sales director / operations director
Selling price	$125.00 per unit	Customer contracts and approved price list	Sales director
Direct material standard	4.0 kg at $8.00 per kg	Bill of materials, supplier quotations, expected normal waste	Procurement / engineering
Direct labor standard	1.5 hours at $24.00 per hour	Time study, staffing plan, wage agreements	Operations / HR
Variable overhead	$10.00 per direct labor hour	Energy, supplies, and support-cost driver analysis	Controller / operations
Fixed manufacturing overhead	$300,000 per quarter	Approved salaries, depreciation, occupancy, maintenance contracts	Controller / plant manager
Minimum cash balance	$75,000	Liquidity policy and downside analysis	CFO / treasury
Variance investigation rule	Greater of $5,000 or 3%; all quality and compliance exceptions	Management-control policy	CFO / quality director

Note. The standards are attainable expectations that include normal operating conditions. They are not perfect-efficiency targets.

Opening Quarterly Operating Budget

Budget Item	Calculation	Quarterly Amount
Sales revenue	10,000 units x $125	$1,250,000
Direct materials	10,000 units x 4.0 kg x $8	(320,000)
Direct labor	10,000 units x 1.5 hours x $24	(360,000)
Variable manufacturing overhead	15,000 labor hours x $10	(150,000)
Contribution margin	Revenue less variable manufacturing cost	$420,000
Fixed manufacturing overhead	Quarterly fixed-cost plan	(300,000)
Budgeted operating income	**Contribution margin less fixed overhead**	**$120,000**

Note. Selling and administrative costs are excluded from this product-line baseline so that the later manufacturing variance analysis uses the same controllable cost structure.

Unit-Economics Measure	Result
Selling price per unit	$125.00
Variable manufacturing cost per unit	$83.00
Contribution margin per unit	$42.00
Contribution-margin ratio	33.6%
Break-even volume	7,143 units
Margin of safety	2,857 units / 28.6%
Degree of operating leverage at plan	3.50

The baseline provides a clear profit model. Each additional unit sold above break-even contributes $42 before any change in fixed cost. The 3.50 degree of operating leverage means that operating income is sensitive to volume near the planned level. Management should therefore test volume assumptions before approving discretionary spending or capital commitments.

Volume Sensitivity and Planning Range

Scenario	Units	Revenue	Variable Cost	Contribution Margin	Fixed Cost	Operating Income
Downside	9,000	$1,125,000	$747,000	$378,000	$300,000	$78,000
Base plan	10,000	1,250,000	830,000	420,000	300,000	120,000
Upside	11,000	1,375,000	913,000	462,000	300,000	162,000

Note. The sensitivity assumes the $125 selling price, $83 variable cost per unit, and $300,000 fixed manufacturing cost remain unchanged within the relevant range.

A 10 percent volume reduction lowers operating income by $42,000, or 35 percent, because fixed cost does not fall with activity in the short term. The downside case still produces a profit, but the smaller cushion makes cash collections, inventory, and discretionary spending more important. The sales forecast should therefore include probability-weighted scenarios rather than a single optimistic number.

Planning Methods and Budget Type

Method	Strength	Risk	Meridian Application
Participative budgeting	Uses operational knowledge and improves ownership.	May create slack or local optimization.	Managers propose assumptions; finance benchmarks and challenges them.
Top-down targets	Keeps the plan aligned with strategy and affordability.	May be unrealistic if operating constraints are ignored.	Executives set outcome ranges, not unsupported line-item cuts.
Rolling forecast	Extends the outlook and responds to new information.	Can blur accountability if forecasts replace the approved budget.	Preserve the original budget and show forecast changes separately.
Flexible budget	Evaluates variable costs at actual activity.	Requires reliable cost behavior and drivers.	Use actual units and hours after month-end.
Zero-based review	Challenges legacy discretionary spending.	Time-consuming and unsuitable for every account each cycle.	Apply to selected overhead and projects on a rotating basis.
Driver-based planning	Links resources to units, hours, kilograms, orders, or customers.	Poor drivers can give false precision.	Validate drivers with operations and historical evidence.

The recommended design is hybrid. Strategic and financial limits come from senior management, but the detailed forecast is built with responsible managers. The approved static budget communicates the commitment made before the period. A flexible budget then adjusts variable revenue and cost expectations to actual activity for fair performance evaluation. OpenStax explains that flexible budgets adjust variable amounts to the actual level of activity, which makes them more useful for cost control than a static comparison alone (Franklin et al., 2019).

Integration of Operating and Financial Budgets

Budget Schedule	Key Inputs	Main Link
Sales budget	Units, price, product mix, customer timing	Production and collection schedules

Budget Schedule	Key Inputs	Main Link
Production budget	Sales plus desired ending inventory less beginning inventory	Materials, labor, overhead, capacity
Resource budgets	Quantity and rate standards for materials, labor, and support activities	Cost of production and cash payments
Operating expense budget	Selling, administrative, quality, technology, and compliance resources	Budgeted operating income
Capital budget	Asset cost, timing, benefits, risk, and approval gates	Depreciation, cash, financing, capacity
Cash budget	Collections, supplier payments, payroll, overhead, taxes, capital spending, and debt	Borrowing, investing, and minimum cash
Budgeted statements	Income statement, balance sheet, and cash flow	Complete financial feasibility check

A profitable operating budget can still fail if customer receipts occur after payroll, supplier, or capital payments. Financial budgets must therefore test liquidity and financing by month or quarter. OpenStax notes that cash budgets are commonly prepared for short periods so management can identify timing shortages and financing needs (Franklin et al., 2019). Meridian should maintain a 13-week cash forecast in addition to the annual plan when collections, purchases, or capital spending are volatile.

Performance Measures and Review Rules

Perspective	Measure	Frequency	Owner
Financial	Revenue, contribution margin, operating income, cash balance	Monthly	CFO / controller
Demand	Order intake, backlog, forecast accuracy, price realization	Weekly / monthly	Sales director
Materials	Price per kg, material usage per unit, scrap and supplier defects	Weekly / monthly	Procurement / plant manager
Labor	Hours per unit, overtime, training completion, absenteeism	Weekly / monthly	Operations / HR
Quality	First-pass yield, rework, complaints, calibration failure	Daily / monthly	Quality director
Delivery	Schedule attainment and on-time delivery	Weekly / monthly	Operations
Liquidity	13-week cash forecast, minimum cash, borrowing and covenant headroom	Weekly / monthly	Treasury
Control	Late approvals, unauthorized changes, unresolved actions, access exceptions	Monthly / quarterly	Controller / internal audit

Note. Investigate a financial variance when it exceeds the greater of $5,000 or 3 percent. Escalate every material quality, safety, compliance, cybersecurity, or suspected-fraud issue regardless of the amount.

Variance review should focus on cause and response rather than blame. Finance should first distinguish volume from execution by preparing a flexible budget. Managers then classify the cause as price, quantity, efficiency, capacity, timing, mix, quality, or an external factor. Every significant exception requires an owner, corrective action, due date, expected financial effect, and evidence of closure.

Internal Control and Data Governance

Control Area	Risk	Required Control
Assumption approval	Unsupported or biased inputs	Source document, named owner, finance review, CFO approval
Model integrity	Broken formulas or inconsistent schedules	Protected formulas, reconciliation checks, independent review
Version management	Managers use different budget files	Central repository, controlled naming, timestamp, approved baseline
Access management	Unauthorized change to assumptions or vendor data	Role-based access, segregation of duties, access review
Capital authorization	Commitments exceed approved limits	Business case, bid review, authority matrix, milestone payments
Actual-data interface	Incorrect general-ledger or operational data	Automated interfaces, reconciliations, exception reports
Management override	Targets or results are changed without evidence	Change log, executive approval, audit-committee visibility
Monitoring	Actions remain unresolved	Monthly action log and quarterly internal-audit follow-up

COSO states that its Internal Control - Integrated Framework is intended to improve confidence in organizational data and information (Committee of Sponsoring Organizations of the Treadway Commission [COSO], 2013). Meridian should apply the framework to budgeting by establishing clear authority, assessing forecast and fraud risks, designing preventive and detective controls, maintaining reliable information flows, and monitoring whether controls operate as intended.

Ethical and Behavioral Considerations

Behavioral Risk	Example	Safeguard
Budgetary slack	Managers understate revenue or overstate cost to make targets easier.	Benchmark assumptions, require evidence, and compare forecasts with later outcomes.
Short-termism	Maintenance, training, or quality work is delayed to meet profit targets.	Use quality and risk measures alongside financial results.
Cost shifting	Expenses are moved between periods or departments.	Accrual review, cutoff testing, and consistent responsibility rules.
Forecast manipulation	The forecast is changed after poor performance to hide the original commitment.	Report approved budget, current forecast, and actual results separately.
Unfair accountability	Managers are judged for volume, prices, or events they cannot control.	Use flexible budgets and document controllability before assigning responsibility.
Suppressed information	Bad news is omitted from executive or board reporting.	Protected escalation route, objective reporting, and audit-committee access.

The IMA Statement of Ethical Professional Practice emphasizes competence, confidentiality, integrity, and credibility. Management accountants should communicate information fairly and objectively and disclose information that could influence a user's understanding (Institute of Management Accountants, n.d.). Finance should not approve a budget it knows is impossible, hide a liquidity problem, or present forecast savings as completed results.

Implementation Roadmap

Timing	Action	Accountable Owner
Weeks 1-2	Approve budget policy, objectives, calendar, roles, thresholds, and system access.	CFO and executive team
Weeks 3-4	Create assumptions register; gather demand, capacity, supplier, labor, and cash evidence.	Controller and budget owners
Weeks 5-6	Build linked sales, production, resource, operating, capital, and cash schedules.	FP&A / treasury
Week 7	Perform downside, base, and upside scenarios; test capacity, liquidity, and covenant limits.	Finance and operations
Week 8	Conduct cross-functional challenge meeting and resolve inconsistencies.	Executive team
Week 9	Approve and lock the baseline budget; distribute scorecards and accountability statements.	CEO / CFO / board
Monthly	Issue actual-versus-flexible reports and manage corrective-action log.	Controller and managers
Quarterly	Refresh the rolling 12-month forecast and report risks to the board.	CFO / board

Recommendation

1. Approve the seven-stage planning framework and make the CFO accountable for maintaining one controlled master budget.
2. Adopt the 10,000-unit opening quarterly budget as the baseline for the portable cardiac-monitor line, subject to final validation of the sales pipeline and production capacity.
3. Use a rolling 12-month forecast for current decisions while retaining the approved budget as the original performance commitment.
4. Evaluate operating performance with a flexible budget at actual volume and investigate the greater of $5,000 or 3 percent, with automatic escalation of quality, safety, compliance, cybersecurity, and suspected-fraud concerns.
5. Integrate cash, capital, and financing schedules before approving spending so that a profitable plan cannot create an avoidable liquidity crisis.
6. Use the COSO control structure, the IIA accountability model, and the IMA ethical standards to protect data integrity, fair evaluation, and transparent reporting.

Conclusion

Meridian's budget should be a disciplined decision system rather than an annual spreadsheet exercise. The proposed framework links strategy, documented assumptions, operating schedules, cash and capital planning, approval, performance review, and continuous forecasting. The opening budget indicates $120,000 of quarterly operating income at 10,000 units, but the sensitivity analysis shows that profit can change quickly when volume moves. Participative planning, flexible-budget evaluation, strong controls, nonfinancial quality measures, and ethical reporting give management a practical basis for protecting margin without sacrificing product quality or organizational credibility.

References

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Appendix A: Key Calculations

Measure	Formula	Result
Variable cost per unit	$32 materials + $36 labor + $15 variable overhead	$83.00
Contribution margin per unit	$125 selling price - $83 variable cost	$42.00
Contribution-margin ratio	$42 / $125	33.6%
Break-even units	$300,000 fixed cost / $42 contribution margin	7,143 units
Margin of safety in units	10,000 planned units - 7,143 break-even units	2,857 units
Margin of safety percentage	2,857 / 10,000	28.6%
Degree of operating leverage	$420,000 contribution margin / $120,000 operating income	3.50

Appendix B: Assessment Coverage Map

Course-Aligned Requirement	Location in Sample
Explain a complete budget planning framework.	Budget Planning Framework; Integration of Operating and Financial Budgets
Develop and support budget assumptions.	Baseline Planning Assumptions
Prepare and interpret a quantitative operating budget.	Opening Quarterly Operating Budget; Key Calculations
Evaluate sensitivity, profitability, and planning risk.	Volume Sensitivity and Planning Range
Recommend governance, controls, and accountability.	Governance and Responsibility; Internal Control and Data Governance
Address behavioral and ethical budgeting issues.	Ethical and Behavioral Considerations
Provide a practical implementation recommendation.	Implementation Roadmap; Recommendation