Best Practices in Budgeting

October 10, 2019
Why Budgeting?

- More than just a financial exercise
- Bringing the goals and strategies of a district to fruition
- Making connections between desired and required services/outcomes and the dollars
GFOA’s Budgeting Best Practices

- Strategic and Long Term Planning
  - Forecasting
- Fund Balance
- Budget Process
  - Capital Budgeting
  - Personnel Budgeting
  - Performance Management
  - Internal Services
  - Pension and Health Care Costs
  - Charges and Fees
  - Budgeting for School Districts and Community Colleges
- Budget Document

https://www.gfoa.org/best-practices
Key Characteristics of the Budget Process:

- Incorporates a long-term perspective
- Establishes linkages to broad organizational goals
- Focuses budget decisions on results and outcomes
- Involves and promotes effective communication with stakeholders
- Provides incentives to government management and employees

Strategic and Long Term Planning
Establishment of Strategic Plans
Long-Term Financial Planning
Financial Forecasting in the Budget Preparation Process
Inflationary Indices in Budgeting
The Use of Trend Data and Comparative Data for Financial Analysis
“Good financial planning without aspirations is accounting. Great aspirations without financial planning is a recipe for disaster.”

- Former Minneapolis Mayor R.T. Rybak
Plans vs. Planning

“Plans are nothing, planning is everything”
- General Dwight D. Eisenhower
The Connections

GOALS

- Strategic plan
- Long-term financial plan
- Capital plan
- Budget
- Results evaluation

DIRECTION

EXPECTATIONS
What is Strategic Planning

Strategic planning is an organizational, management activity used to set priorities, focus energy and resources on goals, establish agreement on outcomes and results, and assess and adjust the organization to a changing environment.
Why focus on strategy?

- Strategy is designed to implement change
- Strategy informs how the people, activities and resources support the instructional core
- Strategy positions the organization to realize critical outcomes and accomplish the mission and vision
Collaborative & Participative Process

- Process must engage different groups to:
  - Gain different vantage points
  - Increase plan quality
  - Build a wide basis of support for strategies

Do this by linking to service priorities
Strategic Planning – Key Steps

1. Initiate the process
2. Prepare a mission statement
3. Assess environment
4. Identify critical issues
5. Agree on limited number of broad goals
6. Develop strategies to achieve goals
7. Create action plan
Strategic Planning – Key Steps
(continued)

8. Develop measurable objectives
9. Incorporate performance measures
10. Obtain approval of plan
11. Implement plan
12. Monitor progress
13. Reassess strategic plan

GFOA Best Practice - http://www.gfoa.org/establishment-strategic-plans
Strategic Planning – Breakdown

What is our purpose? What do we do?

What is our picture of the future?

What results do we want to satisfy our customer/stakeholder needs?

What are the main focus areas (“Pillars of Excellence”) of our business?

What continuous improvement activities are needed to get results?

How will we evaluate performance to know if we are achieving the results we want?

Specifically, what projects and programs will lead to the desired results?

Customer/Stakeholder Needs

Mission

Vision

Strategic Goals

Strategic Priority Areas/Themes

Objectives

Measures & Targets

Strategic Initiatives

35,000 ft.

25,000 ft.

15,000 ft.

Ground

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Customer/Stakeholder Needs
“Enough with all the strategic planning. Get out there and kill something.”
The Strategic Plan and the Budget Process

- Strategic plans should set relative priorities (everything can’t be of equal value)
- Strategic plans may include organizational goals, potentially down to the department or main functions level
- But - the budget process must allocate limited resources and inherently results in prioritization
- Thus, a strategic plan will help with, but does not substitute for, a budget process
- The budget process should have results consistent with the objectives of the strategic plan
The Strategic Plan

- A strategic plan documents the results of a strategic planning process.
- The plan provides a set of policies and actions intended to achieve goals or objectives.
- The plan should generally identify the approach for what services are to be delivered and what infrastructure/capital is to be provided and how.
- The budget should be the implementation of the short-term aspect of that strategy.
Long-Term Financial Planning and Strategic Planning

- A long-term financial plan can be integrated into an overall strategic plan or it can be separate
- The approach taken should be what works well for the organization
- What works well now will change over time as threats and opportunities occur
Long-term financial planning is a process that identifies approaches to help make resources available in the long-term to achieve or more closely achieve organizational service and infrastructure goals through use of multi-year financial information, including forecasting.
Why?

- Identifies future financial opportunities and threats
- Provides a basis for discussion of and for addressing them, hopefully in a timely manner
- Provides a framework for financial decisions and for annual budgets
- May help avoid major financial and political problems
Typical Components

- A forecast of five to ten years (at least for General Fund – work to add other operating funds)
- Factors impacting major relevant revenue sources
- Factors impacting major expenditures (operating and capital)
- Review of financial (and other) policies and their impact
- Identifying and addressing threats and opportunities
Strategic Financial Planning Process

- **Strategic Planning**
  - Identify & Confirm Critical Issues
  - Analyze Financial Trends, Debt, & Develop Forecasts
  - Identify Imbalances
  - Financial Strategy Workshop
    - Prepare Strategic Financial Plan
    - Implement & Monitor
  - Implement through Budget

**KEY**
- Staff Task
- Board & Staff Task
- Board & Staff Task with Critical Point of Public Input

Deliberate & Approve Critical Assumptions
The Five Pillars of LTFP

- Successful long-term financial plans (LTTFPs) share the following characteristics:
  - Long-term service vision
  - Financial policies
  - Technically sound analysis & forecasting
  - Collaborative & participative process
  - Connection to other plans
Forecasting

- Includes: revenues, expenditures, structural balance, fund balances, and reserves
- Describe major assumptions, e.g., maintain services, no recession, current growth trends, COLA wage increases
- Describe forecasting limitations and have an approach, e.g., represents only the trends, use ranges, etc.
- Understand major changes and issues that will or may happen and need to be modeled
- May well have more than one forecast, e.g., no recession scenario, recession scenario
What-If Scenarios

- May help credibility
- Can be used for ranges of projections
- Will help explain threats and opportunities
- But scenarios introduce complexity and can create confusion
- Experiment and see what works best
But, a Forecast is **not** the Goal

- A forecast only provides background information
- Goal is to paint a picture of alternative financial futures and develop options and recommendations to get to the desired future
- Detail and exhaustive analysis in the main report is likely a mistake
- Credibility and politics will likely play key roles
Be Practical and Look to the Future

- What works for the organization (guess!)
- Integrate with other planning or projection processes
- May need to be incremental
- An achieved smaller benefit is better than an unachieved great theoretical benefit
- The budget process is often a great place to start
Presentation is Important

- **Expenditures** were greater than revenues during the Great Recession, but we now have them stabilized.

- **Revenues** have recovered and our best estimate is for steady growth.

We are 90% confident revenues will fall between these lines.

**Forecast**

- **Reserves at Year End as Percent of Annual Expenditures**
The Dreaded Shelf

- Why does it happen and what can be done to prevent it?
- Does it belong on the shelf?
- What keeps it on the shelf?
- Is being on the shelf all bad, i.e., does it still have a use while sitting there?
Integrating Financial Planning and Strategic Planning

- A long-term financial plan can be integrated into an overall strategic plan or it can be separate.
- The approach taken should be what works for the organization and the opportunities that present themselves.
- Always watch for opportunities and take the initiative as a leader.
- Don’t let short-term set-backs stop you.
FINANCIAL FOUNDATIONS

Pillar 1
ESTABLISH LONG-TERM VISION
Give people a reason to cooperate.

Pillar 2
BUILD TRUST AND OPEN COMMUNICATION
Create the conditions for cooperation.

Pillar 3
USE COLLECTIVE DECISION MAKING
Develop forums for participation.

Pillar 4
CREATE CLEAR RULES
Reinforce constructive behavior.

Pillar 5
TREAT EVERYONE FAIRLY
Promote and protect mutual trust and respect.

https://www.gfoa.org/financialfoundations/
Fund Balance
GFOA Best Practices

- Fund Balance Guidelines for the General Fund
- Achieving a Structurally Balanced Budget
- Working Capital Targets for Enterprise Funds
Fund Balance Guidelines for the General Fund

- Why have a fund balance guideline?
- GAAP versus budgetary basis
- Appropriate level

https://www.gfoa.org/financial-policy-examples-general-fund-reserves
Why?

- Mitigate current and future risks
- Ensure stable tax rates
- Reserve consistency regardless of administration or governing body
GAAP vs Budget

Key items to keep in mind:

- **GAAP** financial statements utilize five separate categories of fund balance - *nonspendable fund balance, restricted fund balance, committed fund balance, assigned fund balance, and unassigned fund balance.* **Budgetary** fund balance typically represents the total amount accumulated from prior years at a point in time.

- How sub-funds are shown - **GAAP** fund balance includes amounts from all of the sub-funds. **Budgetary** fund balance typically does not.

- Timing of the recognition of revenues and expenditures — **Budget** often recognizes encumbrances arising from purchase orders as expenditures. **GAAP** does not for the preparation of GAAP financial statements.
Recommendation

- Establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund for GAAP and budgetary purposes.
- Guideline should be set by the appropriate policy body.
- Articulate a framework and process for how the government would increase or decrease the level of unrestricted fund balance over a specific time period.
- Provide broad guidance in the policy for how resources will be directed to replenish fund balance should the balance fall below the level prescribed.
Appropriate Level

GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted budgetary fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures.
But more importantly…

- What are your organization’s unique circumstances:
  - Predictability of revenues and the volatility of its expenditures
  - Exposure to significant one-time outlays - disasters, immediate capital needs, state budget cuts
  - Drain upon general fund resources from other funds
  - Potential impact on the entity’s bond ratings and resulting increased interest costs
  - Commitments and assignments of unrestricted fund balance for a specific purpose
Use and Replenishment

- Define conditions that would allow use of fund balance
- Plan to replenish if fund balance falls below required level
- Also, policy should include how funds in excess of policy would be used
Budget Process
GFOA Best Practices

- **Budget Monitoring**
- Adopting Financial Policies
- Public Engagement in the Budget Process
- Multi-Year Capital Planning
- Capital Budget Presentation
- Effective Budgeting of Salary and Wages
- Role of the Finance Officer in Collective Bargaining
- **Performance Measures**
- Pricing Internal Services
- Strategies for Managing Health-Care Costs
- Sustainable Funding Practices for Defined Benefit Pensions and Other Postemployment Benefits (OPEB)
- Establishing Government Charges and Fees
- Best Practices in Community College Budgeting
- Best Practices in School District Budgeting
What is Monitoring?

“A formal set of processes for comparing budget to actual results to monitor financial performance. Budget monitoring should include analysis of a diverse set of indicators to best inform the analysis and facilitate evaluation of a government’s overall performance. Establishing and conducting regular budget monitoring provides organizations the opportunity to promptly adjust for any significant variances to ensure continuity of program/service delivery.”

GFOA Best Practice - [http://www.gfoa.org/budget-monitoring](http://www.gfoa.org/budget-monitoring)
Essential Components

- Identify elements to be reviewed
- How to analyze elements
- Level of detail for analysis
- Responsibility for analysis
- Tools for conducting analysis
- Communicating analysis
- Action/next steps
Elements to Review

- **Revenues**
  - Key considerations:
    - Seasonality
    - Volatility
    - Trends/comparison to projections
    - One time sources
    - Timing
    - Economic indicator relationship
    - Impact of overarching governments
    - Experiences of peers

- **Expenditures**
  - Key items:
    - Personnel – expenses, hiring, fringe benefits
    - Non-personnel – expenses, encumbrances, etc.
    - Operations - are things on track?
    - Capital
    - Economic trends
    - Performance measures – discussed more shortly...
Analyzing Elements

- Root cause – the “Why?”
- Time frame – one-time? Accelerated?
- Other reporting requirements
- Basis of comparison – ensure logical/relevant. Start with budget vs. actual. Expand to include:
  - Previous year actuals
  - Averages of several prior year actuals
  - Projections and forecasts
Level of Detail

- Vary depending on type – should mirror chart of accounts:
  - **Fund**. High level analysis. May be the only monitoring needed for minor revenue/expenditure areas.
  - **Department**. Establishing budget accountability.
  - **Sub-department/division**. For budget accountability, depending on structure of organization.
  - **Function**. Organizational responsibilities.
  - **Object/account**. Key types of expense, i.e. overtime
  - **Project/program/grant/activity**. Specific activities that require additional scrutiny or for reporting purposes
Responsibilities/Roles

- Clearly identify who produces what
- Ensuring collaboration to provide context
- Identify responsibilities for resolving variances in spend, service delivery, or any other items needing attention
Tools for Conducting Analysis

- Leverage the organization’s electronic/enterprise resource planning (ERP) system for data gathering and analysis to greatest extent possible
- Integrate budget monitoring data and reports into the organization’s ERP system to ensure efficiency and consistency
- Ensure mechanisms are in place to prevent overspend within their ERP system and provide notification
- Any off-system analysis should be consistently applied and clearly articulated to both staff conducting the analysis and end users
Communicating Analysis

- **Frequency** – may vary, should be agreed upon
- **Delivery** of monitoring information – agree upon completion, provide to internal and external stakeholders
- **Format** – how to provide information, including considerations for audience and their level of expertise
- **Transparency** – how best to share on wide basis and include proper context to minimize requests for further clarification
Action/Next Steps

- Continuous improvement
- Responsibilities for resolving issues
- Timeline for resolving
- Ensuring resolution
What are Performance Measures?

“Performance measures are used by governments to collect information about operational activities, achievement of goals, community conditions, or other environmental factors to better understand a situation and make informed decisions. Regardless if an organization has a centralized collection system for performance measures, the use of performance data should be integral to an organization’s decision making processes and leaders within an organization should set expectations that key decisions are supported by evidence. For optimal use, performance measures need to be developed considering the potential audience for the information. As a result, organizations need to identify and track measures at an operational, managerial, policy making, and community level.”

GFOA Best Practice - [http://www.gfoa.org/performance-measures](http://www.gfoa.org/performance-measures)
Key Conditions

- Useful
- Relevant
- Reliable
- Adequate
- Collectible
- Consistent
Less Obvious Conditions

- Environment – externalities impacting services
- Responsibility – who collects, stores and disseminates
- Systems – leverage systems appropriately or identify need for new systems to ease burden of collection
Comparisons Are Tricky

- Comparing/benchmarking measures with other organizations can lead to misinterpretation.
- Problems include unique environments, different measurement approaches, different ways of measuring, and differing service levels.
Communicating Performance Measures *Internally*

- **Expectations** – how utilized
- **Purpose** – inform decision-making and understanding
- **Clarity** – include expected results/targets and actual results
- **Data integrity** – how data used/interpreted should be clearly articulated
- **Context** – provide background on why selected
- **Production** – reference sources
- **Dissemination** – wide distribution and made readily available
Communicating Performance Measures *Externally*

- **Delivery** – how and where
- **Audience** – identify primary audience
- **Format** – best way to present
- **Frequency** – how often
- **Clarity** – explain source of the data, how the calculations were conducted and why, and what the performance measures show
- **Context** – why were these measures chosen, why target measures were set, and what the results mean to operations, service levels, or community outcomes.
Performance Measures are a Function of Time

What are the data trends?
What projections did we get wrong?
What factors have impacted performance?

What is happening now?
How does that compare with the past?
Are service levels meeting goals?
How does our progress compare to other communities?

What is the impact on tomorrow?
Budget Document
GFOA Best Practices

- Basis of Accounting versus Budgetary Basis
- Departmental Presentation in the Operating Budget Document
- The Statistical/Supplemental Section of the Budget Document
- Capital Budget Presentation
- Accurately Displaying Total Expenditures in Budget Presentations (Budget Consolidation)
- Making the Budget Document Easier to Understand
Questions?

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