

Budget Creation and Monitoring

Budgets are an agency's tool for linking near-term goals with the resources available to achieve them, while keeping in mind long-term goals and resources and how the agency's annual budget fits into its capital plan. Budgeting typically involves:

1. Establishing goals and priorities for the agency;
2. Allocating resources according to those goals and priorities; and
3. Comparing actual expenses and revenues to those estimated in the current budgeted expenses, making adjustments during the course of the budget year as necessary.

As important of a function as budgeting is, decision-makers may find that their options are limited in determining how the agency's monies are actually spent. The limitations may result from legal restrictions on how funds may be used, matching funds issues (that will result in loss of revenues if the agency does not spend a certain amount), and state mandates.

Budgets play the following roles:

- **Financial Plan.** The budget document shows where agency revenues come from and how they are used. It demonstrates an agency's ability to meet recurring expenses with recurring revenues. As the fiscal year proceeds, there may need to be adjustments in the agency's financial plan—the role of elected officials is to understand why such adjustments were necessary and what steps were taken to avoid having to make these adjustments.
- **Communications Tool.** The document also is an opportunity to explain to decision-makers, the news media, staff and the public:
 - What the agency does and why;
 - How the agency is organized to deliver programs and services;
 - The kinds of programs, services and activities planned for the budget period and what kinds of costs are involved;
 - Key fiscal issues facing the agency; and
 - How the agency assesses the efficiency and effectiveness of agency efforts (see also note on performance measurement on page 11).
- **Yardstick.** Once adopted, local officials and others can use budget numbers as a reference against which to compare expenditures and revenues throughout the year. As such, the budget provides an ongoing financial management tool to make sure the agency spends within its means and balances expenses against revenues.

The budget document should be easily understood by the average member of the community. To help make this happen, financial information can be presented a variety of ways (including text, tables and charts). Including performance measures in the budget document can help the public see the relationship between costs and benefits.

Because of the public information role the budget document serves, the Government Finance Officers Association recommends that budget documents be shared via the agency's website.¹

Questions to Ask

Role of Governing Body Members

- Do governing body members have a clear understanding of their role in the budget process?
- Do governing body members have a meaningful opportunity to shape major goals and objectives *before* the preliminary budget is prepared (for example, in budget workshops conducted sufficiently in advance of the preliminary budget's preparation)?
- Do governing body members feel like they have been given an opportunity to understand and react to key decision points within a preliminary budget (versus being subjected to a long, random presentation about numbers)?

General Questions about the Numbers in the Budget

- What are the budget's underlying assumptions (examples of key assumptions include population changes, projected caseloads or service demands, state and federal funding, construction activity, utilities costs, service demands, inflation, and interest rates)? Are these assumptions realistic? What are the potential sources of uncertainty and risks regarding these assumptions?
- Does the budget explain the projections for the most significant general fund revenue sources? (These probably account for close to a large percentage of total general fund revenues.)
- For agencies providing social services, how are caseload and benefit costs forecast and managed?

Budgets Don't Tell the Whole Story

Operating budgets and financial reports do not address many important issues that decision-makers must consider. For example, they do not:

- Show postponed or avoided costs (for example, deferred maintenance on facilities or infrastructure)
- Use of one-time or expiring revenue sources.
- Indicate changes in purchasing power due to inflation or deflation.
- Measure the decline or depreciation of infrastructure (like roads, bridges and sewer lines) and public facilities (like buildings and parks).

Local officials may wish to ask staff to provide an analysis of how these variables affect the agency's ability to deliver services and facilities.

- Does the budget summarize major expenses:
 - By function or program tied to areas of public service(s) or facilities the agency provides?
 - By category? (Examples include capital expenses, debt service, and operating expenses like staffing, contract services, and supplies).
 - By fund type? (Examples include the general fund and various enterprise funds, if the agency has special funds).
- Is the budget balanced by one-time fixes or is there a sustainable long-term funding strategy (this is also an issue to be addressed in the agency's long-term financial planning documents, see page 14)?
- Does the budget clearly show the beginning and ending balances in each fund (fund balances)?
- Is the general fund budget balanced (in other words, are there enough projected revenues to fund estimated expenses)?
- Does the budget use one-time revenues only for one-time expenses (rather than ongoing expenses)?
- Does any fund have a deficit (in other words, is it projected to spend more than it brings in)? Why? Is it the deficit temporary or permanent?
- What are the most significant changes since last year's adopted budget?
- With respect to the agency's general fund, how is the fund balance projected to change?
 - How are other funds' fund balances projected to change?
 - How will any resulting changes affect the agency's compliance with its reserve policies?
- Does the budget compare actual expenses and revenues from past years so decision-makers and the public can understand how the agency's budgeted numbers compared to reality?
- Does the budget show changes in the agency's overall financial condition? What measures of financial condition does it use?

- How does the agency’s budget compare with other agencies in the geographic area (both for the next fiscal year and the trend over the past five years)?
 - If there are differences, what are they and what factors account for the differences? (For example, are other agencies using different assumptions and why?)
 - Is the agency’s budget dependent on any other agencies, in terms of revenues (or expenditures)?
 - Are the other agencies planning changes that should affect the agency’s assumptions?
- Where is the agency in terms of constitutional limits on state and local spending? (In 1979 the California voters in 1979 approved a ballot measure² that limited the growth in state and local spending to a formula tied to increases in population and inflation. Finance professionals sometimes refer to this as the “Gann Limit” named after the ballot measure’s sponsor. Local voters can approve an increase in the formula, for a period of up to years.³)
- If changes to the budget prove necessary during the fiscal year, why are those adjustments necessary? What steps were taken to avoid having to make mid-year changes? What steps can be taken to avoid such changes in the future?

Local Agency Budgeting: Resources for Further Information

Government Finance Officers Association, *Recommended Budget Practices: A Framework for Improved State and Local Budgeting* (1998), available at www.gfoa.org/services/dfl/budget/RecommendedBudgetPractices.pdf

Institute for Local Government, *A Local Official's Guide to Public Engagement in Budgeting* (2010), available at www.ca-ilg.org/public-engagement-best-practices/engaging-public-budgeting.

Personnel-Related Questions

- What procedures does the agency use to forecast and manage projected personnel expenses?⁴ When do labor agreements expire?
- How does the agency set its salary and benefit levels or ranges?
 - Are there salary-setting guidelines available for positions within the agency? Has the agency considered and followed them?⁵
 - Does the agency research and consider salaries and benefits other agencies provide for positions with similar responsibilities in the agency’s geographic area?
 - How are changes in compensation determined? For unrepresented employees not subject to a memorandum of understanding, are changes based on an annual goal-setting and performance review process? What other variables does the agency consider (overall agency fiscal health, public perception, relationship to other agencies’ practices, etc.)?

- Note: If the agency uses employment contracts, carefully consider the potential future fiscal impacts of automatic contract renewals, automatic increases in compensation, and provisions linking compensation increases to third-party contracts. These may hamper the agency's abilities to control its costs in the future.
- Are position vacancies monitored (including length of each vacancy), to determine if salary savings can be achieved, if position actually required, or if service levels are suffering?
- What is the status of the agency's funding for pension and other post-employment benefits liabilities?

Public Information and Transparency

- What processes will the agency use to inform the public about budget issues? What mechanisms will there opportunities will be provided for public input on budget challenges and priorities?

Are the agency's budget and supporting documents made available on the agency's website?⁶

Note about Performance Measurement

"Performance measurement" (which is sometimes known by other names) enables an organization to assess its performance against organizational goals. This can occur as part of the budgeting process or as part of general management practices involving assessing the degree to which an organization's activities and priorities are aligned with pursuit of an organization's mission and strategy. Under either approach, the Government Finance Officers' Association recommends that performance measurement be linked to budget decision-making. See www.gfoa.org/downloads/budgetpermanagement.pdf

More specifically, performance measurement is a management tool for systematically collecting clearly defined data regarding the effectiveness and efficiency of service delivery. The initial questions for elected officials to ask are:

- 1) Whether and how the agency uses performance measurement to assess its activities,
- 2) If the organization uses performance measurement, how is the resulting data analyzed and used in management decision-making (including decisions on allocating resources), and
- 3) How are those results communicated to elected officials and the community?

There are a number of good sources on performance measurement for public agencies, including the International County-City Management Association

(ICMA— icma.org/en/results/center_for_performance_measurement/home and the Government)

Finance Officers Association

(GFOA – www.gfoa.org/index.php?Itemid=250&id=479&option=com_content&task=view).

To Access the Institute's resources financial management resources, including the complete version of this booklet, go to <http://www.ca-ilg.org/budgeting-finance>

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The Institute welcomes feedback on resource:

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References and Resources

Note: Sections in the California Code are accessible at leginfo.legislature.ca.gov. Fair Political Practices Commission regulations are accessible at www.fppc.ca.gov/index.php?id=52. A source for case law information is www.findlaw.com/cacases/ (requires registration).

- ¹ GFOA Recommended Best Practice: Using Websites to Improve Access to Budget Documents and Financial Reports (2003), www.gfoa.org/downloads/caafr-budgets-to-websites.pdf . See also www.gfoa.org/downloads/websitepresentation.pdf.
- ² See Cal. Const. art. XIII B (added by Proposition 4 on the 1979 ballot and sometimes referred to as the "Gann Limit" after the ballot measure's leading proponent). See also Cal. Gov't Code § 7900 and following.
- ³ Cal. Const. art. XIII B, § 4.
- ⁴ See GFOA Recommended Best Practice: Managing the Salary and Wage Budgeting Process (2010), www.gfoa.org/downloads/GFOA_ManagingtheSalaryandWageBudgetingProcessBP.pdf.
- ⁵ See, e.g., League of California Cities City Manager Compensation Guidelines, available at www.cacities.org/UploadedFiles/LeagueInternet/91/911307cc-e899-43cb-ba97-7d28bf20640c.pdf
- ⁶ GFOA Recommended Best Practice: Using Websites to Improve Access to Budget Documents and Financial Reports (2003), www.gfoa.org/downloads/caafr-budgets-to-websites.pdf . See also www.gfoa.org/downloads/websitepresentation.pdf.