12: Budgeting and Financial Management: Essential Skills for Local Elected Officials

Trainer(s):
Len Wood
The Training Shoppe:
Len Wood & Associates
www.trainingshoppe.com
Your Agency’s Financial Condition

1. How would you rate your organization’s overall financial health?

   1  2  3  4  5  6  7
   Poor            Excellent

2. Where is your agency in the fiscal cycle? Circle one.
   a) Still in decline.
   b) Bottomed out and starting to level off.
   c) On the rise and returning to normal.
   d) At normal or better.

3. What are the three most important negative trends impacting your budget?
   a.
   b.
   c.

4. What are the three most important positive trends impacting your budget?
   a.
   b.
   c.
## Financial Warning Signs

<table>
<thead>
<tr>
<th></th>
<th>Yes</th>
<th>No</th>
<th>Not Sure</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Qualified auditor’s opinion?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Audit report that is more than six months late?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Outstanding short-term debt not paid back at the end of the fiscal year?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. A two-year trend of increasing short-term debt at the end of the fiscal year?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Expenditures exceeding revenues by more than 5 percent for the fiscal year?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Expenditures exceeding revenues for two consecutive years with the second year’s deficit being larger than the first year’s?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Interfund loans that are outstanding at the end of the fiscal year?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Debt service expenditures exceeding 10% of expenditures?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. Property taxes greater than 90% of the tax limit?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>10. Declining property valuations (two consecutive years in a three-year trend)?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>11. A trend of decreasing tax collections (two consecutive years in a three-year trend)?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>12. Selling assets to balance the budget?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>13. Deferring maintenance expenditures?</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>14. Expenditure, revenue and investment reports late?</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Assessing Financial Oversight

Name ________________________  Date  ________

This survey was developed to help assess the effectiveness of financial oversight within your agency. Please address each statement by allocating points on the answer grid as follows:

• If you agree with the statement, place “X” on the answer grid.
• If you do not agree with the statement, leave it blank.
• If you are unsure or don’t know, place “U” in the answer grid.

Financial System Assessment Inventory

1. The City Council has a mission statement that establishes the overall direction for the city organization.

2. Our City has adopted a financial stabilization policy that specifies the establishment, purpose, use and level of reserve funds.

3. Our budget includes clear, well-written, measurable objectives.

4. Performance measures link directly to objectives.

5. Our budget document is user friendly.

6. We are not reluctant to ask probing questions about City finances.

7. Reserve funds are not used to balance our budget.

8. Significant amounts of money are not hidden in the budget.

9. The City Council periodically (every 3-5 years) rotates audit firms.
10. The City has an effective cash management program.
11. The City Council’s mission statement is linked to clear citywide goals.

12. Our City has adopted a financial policy that identifies the manner in which fees and charges are set and the extent to which they cover the cost of the service provided.

13. The budget objectives challenge people.

14. Contracts have specific objectives and performance measures that are used to manage the contract.

15. Our budget is easy to read and follow.

16. We do not waste time micromanaging.

17. We do not use one-time monies to balance the budget.

18. There is not a significant difference between the original budgeted revenues and the final revenues.

19. The auditor meets with the entire City Council or a council subcommittee to go over the results of the audit.

20. The City has sufficient liquidity to avoid breaking into long-term investments and losing interest.

21. The City Council’s overall goals are known and understandable to staff.

22. Our City has adopted a financial policy that guides the issuance and management of debt. Elements include purposes for which debt may be issued, debt limits, debt service limits and funding of debt.

23. Objectives measure the most significant activities carried out by the City departments.

24. We use performance measures effectively.

25. We have a long-term capital improvements budget (5 to 10 years).
26. Our City Council does not get caught up in the pursuit of trivia.
27. We use non-recurring funds for non-recurring projects.
28. Programs are reviewed after adoption to see if they are achieving their goals.
29. The City Council receives the management letter along with a report from staff indicating how problems will be resolved.
30. Investment advice is received from companies that do not have a financial interest in the investments made by the City.
31. The City Council develops overall goals that are sufficiently specific to guide budget decisions and define the services to be emphasized.
32. Our City Council has adopted a policy limiting (or prohibiting) the use of one-time revenues for on-going expenditures.
33. Our objectives help people understand the purpose of budget programs.
34. People pay attention to performance measure results.
35. The budget message adequately addresses major issues, economic assumptions, problems and opportunities.
36. We do not focus too much energy on short-term problems.
37. Our reserves are maintained at an adequate or better level.
38. We issue or refinance debt only when it results in a significant payback or benefit to the City.
39. We use a competitive process to obtain independent auditors services.
40. Our investment reports indicate whether or not the City is using leverage along with the amount of leverage.
41. The City Council agrees on the City’s top three to five goals.
42. Our government has adopted policies and plans for capital asset acquisition, maintenance, replacement and retirement.

43. There are positive incentives for the accomplishment of objectives.

44. Performance measures are used effectively to support budget requests.

45. Members of the community find our budget document helpful in understanding City finances.

46. Our Council effectively carries out its policy role.

47. The City Council is dedicated to preserving an adequate fund balance.

48. We do not pursue grants that are not affordable.

49. The independent auditors report is submitted on time.

50. Investment reports are timely, adequate and understandable.

51. Our City Council regularly publishes its goals and encourages community discussion and feedback.

52. Our financial policies are reported upon in the budget.

53. Our City Council uses objectives to monitor programs rather than to criticize and posture.

54. Performance measures focus on outcomes (quality and results).

55. Our budget document sufficiently explains new spending requests.

56. Our City Council does not get bogged down in administrative tasks.

57. Reserves are clearly identified in the budget.

58. Before we approve capital projects, monies for operating and maintenance expenses must be budgeted.
59. Our last three audit reports contained unqualified opinions.

60. All our investments are not confined to one investment pool.

**Financial System Assessment Inventory**

<table>
<thead>
<tr>
<th>Item</th>
<th>Financial Topic</th>
<th>Score</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Mission and Goals</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>Financial Policies</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C</td>
<td>Objectives</td>
<td></td>
<td></td>
</tr>
<tr>
<td>D</td>
<td>Performance Measures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>E</td>
<td>Budget Document</td>
<td></td>
<td></td>
</tr>
<tr>
<td>F</td>
<td>Oversight</td>
<td></td>
<td></td>
</tr>
<tr>
<td>G</td>
<td>Reserves</td>
<td></td>
<td></td>
</tr>
<tr>
<td>H</td>
<td>Budget Practices</td>
<td></td>
<td></td>
</tr>
<tr>
<td>I</td>
<td>Audit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>J</td>
<td>Investments</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Ranking should be from highest number of “Xs” to lowest number.**
# Financial System Assessment Inventory

## Answer Grid

<table>
<thead>
<tr>
<th></th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
<th>E</th>
<th>F</th>
<th>G</th>
<th>H</th>
<th>I</th>
<th>J</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>7</td>
<td>8</td>
<td>9</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>11</td>
<td>12</td>
<td>13</td>
<td>14</td>
<td>15</td>
<td>16</td>
<td>17</td>
<td>18</td>
<td>19</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>21</td>
<td>22</td>
<td>23</td>
<td>24</td>
<td>25</td>
<td>26</td>
<td>27</td>
<td>28</td>
<td>29</td>
<td>30</td>
<td></td>
</tr>
<tr>
<td>31</td>
<td>32</td>
<td>33</td>
<td>34</td>
<td>35</td>
<td>36</td>
<td>37</td>
<td>38</td>
<td>39</td>
<td>40</td>
<td></td>
</tr>
<tr>
<td>41</td>
<td>42</td>
<td>43</td>
<td>44</td>
<td>45</td>
<td>46</td>
<td>47</td>
<td>48</td>
<td>49</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>51</td>
<td>52</td>
<td>53</td>
<td>54</td>
<td>55</td>
<td>56</td>
<td>57</td>
<td>58</td>
<td>59</td>
<td>60</td>
<td></td>
</tr>
</tbody>
</table>

## Totals

<table>
<thead>
<tr>
<th></th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
<th>E</th>
<th>F</th>
<th>G</th>
<th>H</th>
<th>I</th>
<th>J</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Total Points ________
Budget and Financial

National League of Cities

by Len Wood
www.training shoppe.com
LenWood@aol.com
Avoiding the Fiscal Mistakes Local Governments Make
“I wish I would have listened a bit more, questioned a bit more, and trusted just a bit less.”

Chairman Thomas Reilly
Orange County Board of Supervisors
1. Fail to Identify and Deal with Fiscal Problems Early On

- Many fiscal problems have their genesis during good times.
- Complacency is at the root of many fiscal problems.
- Limited governing board attention time.
Fiscal Problems - Equilibrium

Let's Spend
Fiscal Problems - Problem State

- Phase I
  - Optimistic Assumptions
  - Capital Projects
  - Grant Lost

- Phase II
  - Revenue Drop
  - Grant Lost

- Lost Revenue
- Capital Projects
- Optimistic Assumptions

Graph showing the decrease in revenue and capital projects over two phases.
Fiscal Problems - Crisis State

- Optimistic Assumptions
- Revenue Drop
- Denial
- Capital Projects
- Grant Lost

Phase I
Phase II
Phase III

Reliance on Balances
Fiscal Problems - Implosion

State

Inside Intervention

Outside Intervention

Denial

Reserves

Depleted

Gap
Recognition of the Problem

Blockages

- Denial
- Hope
- Special Interests
- No Reward
Rectifying the Problem

Mayor

City Manager
Accurate Assessment of the Situation?
What is Your Agency’s Financial Condition?

9. Equilibrium State ___
8. ___
7. ___
6. Problem State ___
5. ___
4. ___
3. Crisis State ___
2. ___
1. ___
0. Implosion State ___

1. Where does your City fit along this scale?
2. Why?
2. Fail to Insist on a Structurally Balanced Budget

- How is the budget balanced?
- Is it balanced with one-time funds?
- How do recurring revenues compare to recurring expenditures?
Structurally Balanced Budgets

On-going Revenues

On-going Expenditures

One-Time Money
Distinguish between Recurring and Non-Recurring Revenue

- **Recurring Revenue**: that portion of revenue that can be reasonably expected to continue year after year with some degree of predictability.
  - Recurring: Property Tax
  - Non-Recurring: Settlement from a Lawsuit
Distinguish between Recurring and Non-Recurring Expenditures

- **Recurring Expenditures**: Recurring expenditures should be those that you expect to fund every year in order to maintain current service levels.
  - Recurring Expenditures: Salaries and Current Expenses.
  - Non-Recurring: General Plan Study
One-Time Budget Fixes

- Use Bond Money
- Use Reserves
- Raid Enterprises
- Misappropriate Grants
- Change the books
Are these Recurring or Non-Recurring?

- Tax increase
- Surplus
- Increased fees
- New grant program
- Savings from freezes
- Savings from voluntary furloughs
- Elimination of a program
- Outsourcing of a program
3. Fail to Guard the General Fund Balance
Fund Balance Issues

- What has been the historical and current level?
- How vulnerable is your revenue base?
- Are big spending expenditures programmed?
- What threats and opportunities exist?
Formulas for establishing

- Equivalent to a fixed number of months of operating expenses
- Equivalent to a percentage of annual operating expenditures
- Equivalent to a percentage of annual operating revenues
- Fixed dollar amount
- Other?
Categories of Fund Balance

- Nonspendable
- Restricted
- Committed
- Assigned
- Unassigned
Appropriate Level of Fund Balance

- For Governments that compare “Unreserved Fund Balance” to Revenues: A minimum of no less than 5 to 15% of regular general fund operating revenues.
Appropriate Level of Fund Balance

- For Governments that compare “Unreserved Fund Balance” to Expenditures: A minimum balance of no less than 8 to 17% of regular general fund operating expenditures.
## General Fund - Fund Balance

<table>
<thead>
<tr>
<th>Population</th>
<th>Number</th>
<th>Low</th>
<th>High</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;10,000</td>
<td>169</td>
<td>-17%</td>
<td>195%</td>
<td>24%</td>
</tr>
<tr>
<td>10,000-24,999</td>
<td>309</td>
<td>-11%</td>
<td>219%</td>
<td>15%</td>
</tr>
<tr>
<td>25,000-49,999</td>
<td>260</td>
<td>-17%</td>
<td>215%</td>
<td>14%</td>
</tr>
<tr>
<td>50,000-99,999</td>
<td>190</td>
<td>-8%</td>
<td>66%</td>
<td>9%</td>
</tr>
<tr>
<td>100,000-199,000</td>
<td>78</td>
<td>-37%</td>
<td>89%</td>
<td>7%</td>
</tr>
<tr>
<td>200,000-299,999</td>
<td>23</td>
<td>-2%</td>
<td>20%</td>
<td>6%</td>
</tr>
<tr>
<td>300,000-499,999</td>
<td>21</td>
<td>0%</td>
<td>38%</td>
<td>6%</td>
</tr>
<tr>
<td>&gt;500,000</td>
<td>15</td>
<td>-8%</td>
<td>17%</td>
<td>3%</td>
</tr>
</tbody>
</table>
General Fund Balance Level
Factors

Cash Flow

Revenue Volatility

Natural Disasters

Insurance Requirements

Lawsuits

Other Natural Events

Ability to Borrow

Non-Recurring Revenue
4. Fail to Appreciate the Financial Cycle

Ever Increasing Upward Trend.
Manage the Financial Cycle

Growing Economy

Recovery

Spiked Revenues

State Takeaways

Recession

Depression
Budgets and Financial Reports

Operating budgets and financial reports are incredibly short-sighted. They do not:

- Project beyond the current period.
- Show postponed and/or avoided costs.
- Indicate reduction of purchasing power due to inflation.
- Measure erosion of infrastructure and public facilities.
Keep the Budget in Balance

Positive Factors
- Unexpected Revenues
- New Revenues
- Fee Offsets
- Expenditure Savings

Negative Factors
- Unexpected Expenditures
- Budget Overages
- Revenue Shortfalls
- Revenue Shortfalls
Plan for the Up and Down Times

- Don’t assume revenues will rise each year.
- Put money aside during peak up years.
- Don’t use surpluses to increase ongoing or new programs recurring expenditures.
- Don’t put surpluses into restoring old spending patterns.
5. Fail to Perform Effective Oversight

Just What is the Oversight Role?
Elected Official Oversight

I honestly did not know the types of questions to ask.

William G. Steiner
Orange County Board of Supervisors
Establish Accountability

Mission, Goals & Measurable Objectives

Financial Policies

Long Range Financial Plan

Capital Improvements Budget

Audit Committee

Investment Policy
Exercise Continuous Oversight

Annual Budget

Audit Report

Treasurer’s Report

Revenue & Expenditure Reports

Supplemental Appropriations

Council Meeting in Progress
Micromanagement is not Oversight

- To micromanage is to manage or control with excessive attention to detail.
- Some micromanagement is innocent and some is not.
Characteristics of Micromanagement

- The public expects us to get involved
- We can’t trust staff
- Look at the mistakes that have been made
- I have experience in this subject
- Detail consumes available time and accomplishes little
- Results in a policy vacuum
- Undermines staff accountability
- Destroys morale
Micromanagement

- Asking questions is not micro-management.
Complacency Management is Just as Destructive

- Complacency management involves oversight from a distance coupled with a lack of on-going monitoring.
Characteristics of Complacency Management

Rationale

- It’s been handled in the past, hasn’t it?
- Trust a little bit.
- It costs too much to hire outside help.
- If it ain’t broke.
- Don’t micromanage.

Indicators

- Lack of concern.
- Receive and file.
- Encourage only good information.
- Don’t bore us.
- Lip service
Being reluctant to ask penetrating questions.

Failing to press when a satisfactory answer is not obtained.

Accepting bold, unsubstantiated statements.

Being obviously supportive in contrast to the treatment of other departments.
Oversight

“In all honesty, I’m not really a finance person.”

Ernie Schneider
Orange County Administrative Officer
Oversight Approaches

Complacency Management

Governing Zone

Micromanagement
What is Your City Council’s Tendency?

Complacency Management

Governing Zone

Micromanagement?

Is Your Council Split over this?
6. Fail to Adopt Meaningful Goals

- Primary Responsibility
- Sets Direction for Organization
- If Not Set a Vacuum is Created
- Staff Fills Vacuum
Why Some Elected Officials Resist Written Goals

- Goals may limit flexibility to change minds when faced with strong pressure.
- Goals may coalesce the opposition once they are publicly expressed.
- Goals may freeze the organization and preclude creativity.
- Goals may not be possible since the elected body cannot agree on the organization's top priorities.
Sure, We Agree

- Franks: Sure, we may have small differences but we agree on the City’s major goals.
- Acero: That is the one thing we can agree on.
- Jelson: The City Council’s goals are clearly delineated in the budget.
## Goal Concurrence?

<table>
<thead>
<tr>
<th>Goal Priority</th>
<th>Franks</th>
<th>Acero</th>
<th>Jelson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Education</td>
<td>Crime</td>
<td>Housing Opportunities</td>
</tr>
<tr>
<td>2.</td>
<td>Industrial Expansion</td>
<td>Police Salaries</td>
<td>Environment</td>
</tr>
<tr>
<td>3.</td>
<td>New Parks</td>
<td>New City Hall</td>
<td>Code Enforcement</td>
</tr>
</tbody>
</table>
## Budgeted Programs

<table>
<thead>
<tr>
<th>Goal Priority</th>
<th>Franks</th>
<th>Acero</th>
<th>Jelson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Education</td>
<td>Crime</td>
<td>Housing Opportunities</td>
</tr>
<tr>
<td></td>
<td><strong>Industrial</strong></td>
<td><strong>Police</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Expansion</strong></td>
<td><strong>Salaries</strong></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>New Park</td>
<td>New City Hall</td>
<td><strong>Code Enforcement</strong></td>
</tr>
</tbody>
</table>

Budgeted programs are underlined.
Mission Statement

It is our job to do the best we can for our customers. Pursuant to that we will provide satisfactory services consistent with our resources.

June 1, 2001
Tips on Developing Goals

- Involve all members of the governing board.
- Negotiate goals.
- Make goals reflective of what you want accomplished.
- Stay away from the detail and the “how to”.
- Be willing to modify goals.
- Do not develop too many goals.
7. Fail to Develop and Enforce Fiscal Policies

- Financial policies establish standards which you can use to oversee operations.
- Example: General Fund on-going revenues will exceed on-going expenditures by 3%.
- Example: General Fund Reserve shall be set at 25% of operating expenditures.
Fiscal Policies Should Be:

- Concise
- Written
- Placed in Budget
- Reviewed and Explained
8. Fail to Understand the Budget Culture

Do you know your organization's budget and financial culture?

Some Examples:
1. Hidden Money
2. Budget Padding
3. Budget Games
4. Pension Spiking
Hidden Money Rationale

- To Provide for Unanticipated Events
- To Keep the Governing Body from Spending it
- To Obscure Controversial Items from the Governing Body and Public
- For Salary Settlements
Budget Padding

Is it acceptable to pad a budget request?

72% Yes
28% No

Dollars & Sense Page 149
Budget Padding

Do you pad your budget requests?

- Yes: 65%
- No: 35%
Dealing with Budget Ploys

- Its only Temporary
- Call out the troops
- Foot in the door
- Washington Monument ploy
Pension Spiking

- Occurs when employees cash in on accumulated sick or leave days right before they retire.
- This increases the total salary at retirement which then inflates the pension payment.
- May need to reform your current plan.
9. Fail to Fully Assess the Limitations of Grants

- Grants must be worth the effort.
- Will the grant reorder priorities?
- Are the strings burdensome?
- Do you have the matching funds?
- Can staff manage it?
- Does it tie to a City goal?
- Key question: What happens when grant funds run out?
10. Fail to Provide for and Protect the Infrastructure

You can pay me now, or you can pay me later.
Fram Oil Filter Commercial
New Project Maintenance

Top of the line $343 million jail stood empty for 14 months.
11. Fail to Evaluate Programs After Adoption

- Did it meet our objectives?
- Do we continue or discontinue the program?
- Can we improve it?
- Should these resources be used for other programs?
Smart Fiscal Management

- Identify and deal with fiscal problems early on
- Insist upon a structurally balanced budget
- Guard the General Fund fund balance
- Recognize the Financial Cycle
- Perform effective oversight
Smart Fiscal Management

- Adopt meaningful goals
- Develop and enforce fiscal policies
- Learn the budget culture
- Assess the limitations of grants
- Provide and care for the infrastructure
- Evaluate programs after adoption
Training Shoppe

Len Wood
4228 Palos Verdes Drive East
Rancho Palos Verdes, CA 90275
310-832-5652
LenWood@aol.com
www.trainingshoppe.com